

CLERK'S COPY.  
Vol. I 163  
TRANSCRIPT OF RECORD

Supreme Court of the United States

OCTOBER TERM, 1942

No. 7

FREDERICK H. ECKER, JOHN W. STEDMAN AND REEVES SCHLEY,  
CONSTITUTING INTERNATIONAL BONDHOLDERS COMMITTEE,  
PETITIONERS, *Interposition*

WESTERN PACIFIC RAILROAD CORPORATION, A. C. JAMES CO.,  
THE RAILROAD CREDIT CORPORATION, ET AL.

No. 8

CROCKER FIRST NATIONAL BANK OF SAN FRANCISCO AND  
SAMUEL ARMSTRONG, AS TRUSTEES UNDER THE WESTERN  
PACIFIC RAILROAD COMPANY FIRST MORTGAGE, DATED JUNE  
26, 1916, PETITIONERS,

vs.

WESTERN PACIFIC RAILROAD CORPORATION, THE WESTERN  
PACIFIC RAILROAD COMPANY, IRVING TRUST COMPANY, ETC.,  
ET AL.

No. 20

THE WESTERN PACIFIC RAILROAD COMPANY, PETITIONER,

vs.

FREDERICK H. ECKER, ET AL.

No. 33

RECONSTRUCTION FINANCE CORPORATION, PETITIONER,

vs.

WESTERN PACIFIC RAILROAD CORPORATION, A. C. JAMES CO.,  
ET AL.

No. 61

IRVING TRUST COMPANY, AS SUBSTITUTED TRUSTEE UNDER  
THE GENERAL AND REFUNDING MORTGAGE OF WESTERN  
PACIFIC RAILROAD COMPANY, PETITIONER,

vs.

CROCKER FIRST NATIONAL BANK OF SAN FRANCISCO, ET AL.,  
ETC.

ON WRITS OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS  
FOR THE NINTH CIRCUIT

PETITIONS FOR CERTIORARI FILED

DECEMBER 30, 1941.
JANUARY 17, 1942.
FEBRUARY 28, 1942.
MARCH 30, 1942.

CERTIORARI GRANTED APRIL 27, 1942.





No. 9714

**United States**  
**Circuit Court of Appeals**

**For the Ninth Circuit.**

In the Matter of,

THE WESTERN PACIFIC RAILROAD COMPANY, a corporation.  
Debtor.

WESTERN PACIFIC RAILROAD CORPORATION, a corporation, THE WESTERN PACIFIC RAILROAD COMPANY, a corporation and IRVING TRUST COMPANY, a corporation, as substituted Trustee under the General and Refunding Mortgage of Western Pacific Railroad Company, A. C. JAMES CO., a corporation, THE RAILROAD CREDIT CORPORATION, a corporation,  
Appellants,

vs.

INSTITUTIONAL BONDHOLDERS COMMITTEE and  
RECONSTRUCTION FINANCE CORPORATION,  
Appellees.

**Transcript of Record**

(Excluding Certain Portions not Printed, in Accordance with  
Stipulation and Order.)

**In Six Volumes**

**VOLUME I**

**Page 1 to 470**

**Upon Appeals from the District Court of the United  
States for the Northern District of California,  
Southern Division.**



## INDEX

[Clerk's Note: When deemed likely to be of an important nature, errors or doubtful matters appearing in the original certified record are printed literally in italic; and, likewise, cancelled matter appearing in the original certified record is printed and cancelled herein accordingly. When possible, an omission from the text is indicated by printing in italic the two words between which the omission seems to occur.]

	Page
Affidavit of service of notice of entry of order approving plan of reorganization.....	1607
Answer of the Institutional Committee to the petition of the Debtor for rehearing and modification of the report and order dated June 21, 1939 of the Interstate Commerce Commission.....	1750
Appeal:	
Designation of contents of record on (appellants') (District Court).....	1618
Designation of contents of record on (Institutional Bondholders' Committee) (District Court).....	1772
Designation of contents of record on (Reconstruction Finance Corp.) (District Court).....	1841
Notices of:	
A. C. James Co. ....	1611
Western Pacific Railroad Corporation.....	1612
Railroad Credit Corporation.....	1613
Western Pacific Railroad Company.....	1616
Irving Trust Company.....	1616

Index	Page
Order dispensing with printing of certain portions of record on.....	2625
Order extending time within which to file transcript of record on (Circuit Court of Appeals).....	2603
Order extending time to file stipulation re portions of record to be printed.....	2607
Statements of points of several appellants on (Circuit Court of Appeals).....	2600
Statements of points relied upon:	
A. C. James Co. (District Court).....	1627
Western Pacific Railroad Corporation (District Court).....	1635
Railroad Credit Corporation (District Court).....	1642
Western Pacific Railroad Company (District Court).....	1645
Irving Trust Co. (District Court).....	1651
Stipulation for order dispensing with printing of certain portions of record on.....	2612
Attorneys of record, names and addresses of.....	1
Clerk's Certificate.....	2596
Commission's order of Sept. 19, 1939 denying debtor's petition for rehearing and modification.....	884
Designation of contents of record (Appellants) (District Court).....	1618

Index	Page
Designation of contents of record—Institutional Bondholders Committee (District Court) .....	1772
Designation of Contents of Record—Reconstruction Finance Corp. (District Court) .....	1841
Exceptions to proposed Report of Bureau of Finance of:	
Railroad Credit Corp. ....	401
Reconstruction Finance Corp. ....	416
Debtor .....	439
Irving Trust Co. ....	486
A. C. James Co. ....	518
Crocker First National Bank .....	573
Institutional Bondholders .....	589
Final modifying report and order of the Commission .....	300
Order .....	362
Memorandum statement, submitted by Reconstruction Finance Corp. in regard to plan of reorganization .....	1764
Monthly Income Statements of debtor (I. C. C. Exhibits 127-148) .....	2239
Names and addresses of attorneys .....	1
Notices of Appeal:	
A. C. James Co. ....	1671
Western Pacific Railroad Corporation .....	1612
Railroad Credit Corp. ....	1613
Western Pacific Railroad Company .....	1616
Irving Trust Co. ....	1616

Index	Page
Notice of entry of order approving plan of reorganization .....	1609
Objections to Interstate Commerce Commission Plan of Reorganization by:	
A. C. James Co. ....	892
Western Pacific Railroad Corporation .....	943
Railroad Credit Corp. ....	955
Western Pacific Railroad Company .....	963
Irving Trust Co. ....	974
Western Realty Co. ....	983
Institutional Bondholders Committee .....	1755
Order approving petition for bankruptcy and restraining disposition of collateral .....	811
Order approving plan of reorganization .....	1600
Order authorizing trustees to extend certificates of indebtedness .....	1834
Order dispensing with printing of certain portions of record on appeal .....	2625
Order extending time to docket .....	1845
Order extending time to docket .....	1846
Order extending time to docket .....	1848
Order extending time to docket .....	1849
Order extending time within which to file transcript of record on appeals .....	2603
Order extending time to file stipulation re portions of transcript of record to be printed .....	2607



*Institutional Bondholders et al.*

Index	Page
Order fixing date of hearing parties in interest	1273
Order fixing time for hearing of petition to extend Certificates of indebtedness	1829
Order for omission and transmission of exhibits	1850
Order making stipulation of facts not in dispute part of record	1273
Opinion of the District Court upon approval of plan of reorganization	1569
Order providing for hearing on petition to borrow \$10,000,000.00	1809
Order relative to issues raised by objections to the Commission plan	1277
Order, supplemental, authorizing the borrowing of \$10,000,000.00 from Reconstruction Finance Corp.	1813
Petition for rehearing and modification of Commission's report and order dated Oct. 10, 1938 by:	
Railroad Credit Corporation	675
Reconstruction Finance Corporation	695
Debtor	702
Irving Trust Co.	708
A. C. James Co.	726
Institutional Bondholders Committee	753
Petition for supplemental order to borrow \$10,000,000.00 from Reconstruction Finance Corporation	1801

Index	Page
Petition of Debtor for rehearing and modification of Commission Report and Order of June 21, 1939 .....	1819
Petition of Debtor under Section 77(a) of Bankruptcy Act .....	4
Petition of Trustees to extend certificates of indebtedness in the amount of \$10,000,000.00 .....	1820
Petition of Western Pacific Railroad Company respecting sale or disposition of collateral by R. F. C., et al. ....	1778
Plan of Reorganization proposed by:	
Debtor .....	19
A. C. James Co. ....	101
A. Basic principles upon which proposed Plan of Reorganization is constructed .....	101
B. General comments as to proposed Plan of Reorganization .....	103
C. Proposed provision for new money and necessary modifications in existing capital structure .....	103
D. Description of new securities .....	108
E. Formation of Reorganization Committee .....	111
F. Method of participation in, and consummation of, the Plan .....	113
G. Expenses of the Plan .....	114

*Institutional Bondholders et al.* vii

Index Page

Schedule A.	
Present Capital Liabilities.....	114

Schedule B.	
Proposed New Capitalization.....	115

Institutional Bondholders Committee.....	48
--	----

Proposed Report of Bureau of Finance of I. C. C. ....	116
--	-----

Replies of the several parties to the exceptions  
of the parties to the proposed report of the  
Bureau of Finance of the Interstate Com-  
merce Commission:

Crocker First National Bank.....	1693
Institutional Bondholders .....	1662
Railroad Credit Corp. ....	1735
Reconstruction Finance Corp.....	1654

Reply of First Mortgage Trustees to the pe- titions for modification of the Interstate Commerce Commission Report and order dated October 10, 1938.....	1745
--	------

Report and Order of the Commission dated Oct. 10, 1938 .....	194
Order .....	281

Report, Final modifying, and order of the Commission .....	300
Order .....	362

Index	Page
Report of the Commission on consideration of petition for further modification of approved plan of reorganization .....	884
Order .....	891
Report, Proposed, of Bureau of Finance of I. C. C. ....	116
Statement of points to be relied upon on appeal (Circuit Court of Appeals) .....	2600
Statements of points relied upon appeal of:	
A. C. James Co. (District Court) .....	1627
Irving Trust Co. (District Court) .....	1651
Railroad Credit Corp. (District Court) .....	1642
Western Pacific Railroad Company (District Court) .....	1645
Western Pacific Railroad Corporation (District Court) .....	1635
Stipulation as to facts not in dispute .....	1017
Exhibits to stipulation of facts not in dispute:	
A. Plan and agreement for reorganization dated December 15, 1915 .....	1112
B. Loan account with the Railroad Credit Corporation .....	1211
C. ....	1214
D. Granting clauses of first mortgage .....	1215

Index	Page
E. Granting clauses of general and refunding mortgage .....	1231
I. Letter dated March 26, 1937 to Irving Trust Company from the Western Pacific Railroad Company .....	1247
J. Standard Realty and Development Company General Balance Sheet as of October 31, 1939 .....	1264
K. High, Low and Total Sales Debtor's First Mortgage 5% Bonds, Six Months' Periods, 1923-1929 .....	1265
L. Total Operating Revenues of the Western Pacific Railroad System and Class I Railroads of the U. S. ....	1267
M. Net Railway Operating Income, Western Pacific Railroad System and Class I Railroads of the U. S. ....	1269
Stipulation for order dispensing with printing of certain portions of record on appeal .....	2612
Supplemental order authorizing the borrowing of \$10,000,000.00 from Reconstruction Finance Corp. ....	1813



Index	Page
Testimony, Transcript of, before District Court .....	1280
Exhibits for Irving Trust Company:	
1-A—Statement headed "Combined Railway Operating Revenues" .....	1302
1-B—Statement headed "Combined income available for interest charges" .....	1304
1-C—Statement headed "Combined income available for interest charges, etc." .....	1305
1-D—Statement entitled, "Gross Revenues accruing to Western Pacific R. R. Co. from freight originating and terminating on and passing over Northern California Extension" .....	1306
1-E—Statement headed "Income available for interest charges Tidewater Southern R. R. Co." .....	1307
1-F—Western Pacific R. R. Co. proportion of revenues over traffic interchange with Tidewater Southern R. R. Co. ....	1308
1-G—"Railway Operating Income, Central California Traction Co." .....	1309



Index	Page
1-H—Income and Profit and Loss, Deficit of Central California Traction Co. ....	1309
1-I—Western Pacific R. R. Co. pro- portion of revenues from traffic interchange with Central Cali- fornia Traction Co. ....	1310
2—Interstate Commerce Valuation of Alameda Belt Line as of De- cember 31, 1935 and December 31, 1938 and also balance sheets of Alameda Belt Line as of said dates .....	1314
4—Statement showing amount of cash and receivables in hands of Trustees on March 4, 1936 .....	1316
5—Statement showing equipment or equity in equipment acquired during course of reorganization proceedings by Debtor's Trustees, etc. ....	1319
6—Listing statement of July 16, 1925 .....	1324
7—Listing statement of September 30, 1926 .....	1350
8—Listing statement of October 31, 1927 .....	1376

Index	Page
9—Listing statement of May 16, 1929	1404
10—Listing statement of July 1, 1930	1433
11—Listing statement of September 30, 1930	1465.
12—Listing statement of February 29, 1935	1496
Exhibits for Petitioners:	
1—Stipulation of Facts and Memoranda of Corrections	1017
Exhibits for Reconstruction Finance Corporation:	
1—Chart headed "Offerings of Railroad bond issues 1938-1940"	1540
2—Table headed "Western Pacific R. R. Co. indicated income remaining after proposed interest charges and per cent of gross revenues of such income remaining, 1922-1938 inc."	1548
Exhibits for Western Pacific Railroad Corporation:	
1—Statement showing percentage of preferred stock of the corporation held by A. C. James Co. and the two corporations which he owns	1529

## Index

## Page

## Witness for Debtor:

Elsey, Charles

—direct ..... 1283

—cross ..... 1289

## Witness for Irving Trust Co.:

Curry, M. J.

—direct ..... 1323

## Witness for Reconstruction Finance Corporation:

Blyth, Charles R.

—direct ..... 1330

Futterer, Charles

—direct ..... 1536

—cross ..... 1557

Testimony, Transcript of, before Interstate  
Commerce Commission

1853

Exhibits introduced before Interstate  
Commerce Commission:

1—Plan of Reorganization effective

January 1, 1936 [Set out at  
page 19] ..... 185922—Western Pacific Railroad Com-  
pany Reorganization Plan fore-  
cast of revenue, expenses and  
income ..... 1922

Index	Page
27—Statements indicating operating revenues of the Western Pacific Railroad Company, preceding the year 1936 and a forecast of those revenues for the years 1936 to 1940, inclusive .....	1950
29—Additional exhibits as requested by counsel for creditors or examiners for Interstate Commerce Commission at hearing held March 23, 1936, together with supplementary explanatory memoranda .....	2020
32—Statements indicating revenues of Sacramento Northern Railway, Tidewater Southern Railway Company and Deep Creek Railroad Company for years 1929 to 1935 inclusive and a forecast of revenues for the years 1936 to 1940 inclusive .....	2121
33—Additional information requested by Examiner Boyden relating to estimates of operating expenses of the Western Pacific Railroad Company as shown by Exhibit 22 .....	2145
38—Report to Frederick H. Ecker, Esq., Chairman of the Board, Metropolitan Life Insurance Co., New York, N. Y. ....	2221

## Index

## Page

- 42—Suggested Plan of Reorganization of the Western Pacific Railroad Company. Effective date January 1, 1937. [Set out at page 48] ..... 2272
- 76—Plan of Reorganization for the Western Pacific Railroad Co. proposed by A. C. James Co. [Set out at page 101] ..... 2407
- 125—Statement showing stockholdings of Arthur Curtiss James in the Western Pacific Railroad Corporation together with the holdings of the Curtiss Southwestern Corporation and the Curtiss Southwestern Company ..... 2565
- 127-148—Monthly income statements of debtor introduced before Commission ..... 2239-2260

## Witnesses before Interstate Commerce

## Commission:

Bon, J. F.

—direct ..... 1927

Buckley, Carl E.

—direct ..... 2349

—recalled, direct ..... 2463

—recalled, direct ..... 2578

—cross ..... 2580

Index	Page
Curry, Michael J.	
—direct .....	1857
—recalled, direct .....	2300
—recalled, direct .....	2433
—recalled, direct .....	2510
De Graff, D. C.	
—direct .....	1999
—cross .....	1999
Elsey, Charles	
—direct .....	1859
—cross .....	1883
—recalled, direct .....	2017
—cross .....	2100
—recalled, direct .....	2195
Engelbright, Edward W.	
—direct .....	1983
—cross .....	1990
—recalled, direct .....	2144
—cross .....	2163
Hamilton, J. A.	
—direct .....	2213
—cross .....	2214
Poulterer, H. E.	
—direct .....	2118
—recalled, cross .....	2191



*Institutional Bondholders et al.*

XVII

Proceedings in U. S. C. C. A., Ninth Circuit	2659
Order directing argument; etc.	2661
Order of submission	2662
Order directing filing of opinion and filing and recording of decree	2663
Opinion, Matthews, J.	2663
Decree of November 28, 1941	2675
Certificate of Clerk of United States Circuit Court of Appeals	2677
Order amending decree of November 28, 1941, etc.	2681
Amended decree	2683
Clerk's certificate	2684
Orders allowing certiorari	2685



## NAMES AND ADDRESSES OF ATTORNEYS

GARRET W. McENERNEY,

ANDREW F. BURKE,

2002 Hobart Building,

San Francisco, California,

WHITMAN, RANSOM, COULSON & GOETZ,

40 Wall Street,

New York, New York.

Attorneys for A. C. James Company.

M. C. SLOSS and

SLOSS & TURNER,

111 Sutter Street,

San Francisco, California,

Attorneys for The Western Pacific  
Railroad Corporation.

EDWARD G. BUCKLAND and

WILLIAM J. KANE,

Maryland Trust Building,

Baltimore, Maryland,

Attorneys for The Railroad Credit  
Corporation.

C. W. DOOLING,

878 Mills Building,

San Francisco, California,

PIERCE & GREER,

40 Wall Street,

New York, New York.

Attorneys for The Western Pacific  
Railroad Company.

FELIX T. SMITH and  
PILLSBURY, MADISON & SUTRO,

Standard Oil Building,  
San Francisco, California,

DAVIES, AUERBACH, CONNELL & HARDY,

1 Wall Street, New York,

Attorneys for Irving Trust Company.

MORRISON, HOHFELD, FOERSTER,

SHUMAN & CLARK,

Crocker Building,  
San Francisco, California,

CRAVATH, de GERSDORFF, SWAINE &  
WOOD,

15 Broad Street,

New York, New York,

Attorneys for Institutional Bondholders  
Committee.

BROBECK, PHLEGER & HARRISON,

Crocker Building,

San Francisco, California,

C. M. CLAY,

1825-H-Street, N. W.,

Washington, D. C.,

Attorneys for Reconstruction Finance Cor-  
poration.

**CHICKERING & GREGORY,**

111 Sutter Street,  
San Francisco, California,

**MILBANK, TWEED & HOPE,**

15 Broad Street,  
New York, New York.

Attorneys for Crocker First National Bank  
of San Francisco and Samuel Armstrong,  
Trustees of First Mortgage of The West-  
ern Pacific Railroad Company.

**FELIX T. SMITH and  
PILLSBURY, MADISON & SUTRO,**

Standard Oil Building,  
San Francisco, California,

**MILBANK, TWEED & HOPE,**

15 Broad Street,  
New York, New York.

Attorneys for Chase National Bank of the  
City of New York.

**THOMAS, BEEDY & PARAMORE,**

315 Montgomery Street,  
San Francisco, California,

Attorneys for Bankers Trust Company

**LEROY R. GOODRICH,**

1001 Bank of America Building,  
Oakland, California,

Attorney for The Western Realty Company.

4      *A. C. James Co., et al. vs.*

In the District Court of the United States,  
for the Northern District of California,  
Southern Division.

23591 S.

In proceedings for the reorganization of a railroad.  
In the Matter of **THE WESTERN PACIFIC  
RAILROAD COMPANY,**

Debtor.

**PETITION [1\*]**

To the Honorable, the Judges of the District Court  
of the United States, for the Northern District  
of California, Southern Division:

The petition of The Western Pacific Railroad  
Company, a railroad corporation, hereinafter re-  
ferred to as the debtor, respectfully represents:

First: That the debtor is a railroad corporation  
organized and existing under the laws of the State  
of California and is a citizen and resident of the  
State of California; and is a common carrier by  
railroad engaged in the transportation of persons  
and property in interstate and intrastate commerce  
in the States of California, Nevada and Utah, and  
is not a street, suburban or interurban electric rail-  
way; that during the six months' period immediately  
preceding the filing of this petition the debtor has  
had, and now has, its principal operating office in  
the City of San Francisco, in the State of Cali-  
fornia, and in the Northern District of California,  
Southern Division.



Second: That there became due on March 1, 1934, interest in the amount of \$1,231,252.50 on \$49,290,100. First Mortgage Bonds of the debtor and a like amount of interest thereon on September 1, 1934, payment of which was conditionally deferred until January 1, 1937, pursuant to a deferment plan agreement signed by holders of more than 86% of the outstanding First Mortgage Bonds, but more than 13% of the holders of said outstanding bonds executed no deferment agreement. That it is provided in [2] the said deferment plan agreement between the debtor and holders of said First Mortgage Bonds, parties to such Deferment Plan, that the installments of interest due March 1, 1934, and September 1, 1934, and conditionally deferred until January 1, 1937, shall forthwith become due and payable if any receiver for The Western Pacific Railroad Company shall be appointed by any Court of competent jurisdiction or any proceeding commenced under Section 77 of the Federal Bankruptcy Act, as amended, prior to January 1, 1937.

That there became due on March 1, 1935, interest in the amount of \$1,231,252.50 on said First Mortgage Bonds of the debtor and the whole amount thereof remains unpaid and the debtor is without funds to pay and discharge the same.

That there is also due and payable the following amounts of interest on the unfunded debt of the debtor and the debtor is without funds to pay and discharge the same:

Name of Creditor	Principal	Interest
	amount of debt as of June 30, 1935	accrued and unpaid as of June 30, 1935
Reconstruction Finance Corporation	\$2,963,000.	\$ 204,324.13
The Railroad Credit Corporation	2,538,956.	53,922.73
A. C. James Co.	4,999,800.	374,985.00
The Western Pacific Railroad Corporation	5,739,722.	1,018,852.76

That the debtor is without funds to pay and discharge the aforesaid obligations as they mature and upon information and belief alleges that it has no means of borrowing or otherwise procuring such funds; that it is unable to meet its debts as they mature and desires to effect a Plan of Reorganization, pursuant to Section 77 of Chapter VIII of the Acts of Congress relating to bankruptcy.

Third: That a Plan of Reorganization of debtor, an outline of which is annexed hereto, marked Exhibit A, has been prepared by the debtor after protracted negotiation and conference [3] with representatives of large institutional holders of First Mortgage Bonds and junior creditors, including Reconstruction Finance Corporation.

Fourth: That a copy of this petition is this day being filed with the Interstate Commerce Commission with a request that said Commission fix an early date for a public hearing at which the debtor may present said Plan, as provided in said Section 77.

Fifth: That the filing of this petition by and on behalf of the debtor was duly authorized by resolution of the Board of Directors of the debtor adopted

at a meeting thereof duly held on the 2nd day of August, 1935.

Wherefore, your petitioner prays that an order may be entered approving this petition as properly filed under said Section 77 of said Chapter VIII and that it be granted all other and further relief to which it may be entitled.

**THE WESTERN PACIFIC RAIL-  
ROAD COMPANY.**

By (original signed) CHARLES ELSEY,  
President.

WARREN OLNEY, Jr.,  
Balfour Building,  
San Francisco, California,  
PIERCE & GREER,  
15 Broad Street,  
New York City, New York.

Attorneys for Debtor. [4]

State of California,  
City and County of San Francisco—ss.

Charles Elsey, being duly sworn, deposes and says, that he is an officer, to wit, the President, of The Western Pacific Railroad Company, a corporation, the petitioner debtor mentioned and described in the foregoing petition; that he has read the foregoing petition and knows the contents thereof; that the same is true of his own knowledge, except as to the matters therein stated on informa-

tion and belief and as to those matters he believes them to be true.

**CHARLES ELSEY.**

Subscribed and sworn to before me this 2nd day of August, 1935.

(Seal)

**FLORA HALL**

Notary Public in and for the City and County of San Francisco, State of California.

My commission expires May 5, 1937.



**THE WESTERN PACIFIC RAILROAD COMPANY  
A PLAN OF REORGANIZATION**

**EXISTING CAPITALIZATION AND OTHER CAPITAL LIABILITIES**

**PROPOSED NEW CAPITALIZATION**

(As of December 31, 1934, except as noted.)

		Equipments to be Undisturbed	Fixed 4% Interest 30-Year First Mortgage Bonds	Fixed 4-4½% Interest 30-Year First Mortgage Bonds (Note 1)	Series "A" 5½% 30-Year Mortgage Income Bonds (Note 2)	Series "B" 5½% 50-Year Mortgage Convertible Income Bonds (Note 2)
<b>Existing Capitalization</b>						
\$ 2,994,065	Equipment Trusts and Baldwin Lease (June 30, 1935)	\$2,994,065	\$ —	\$ —	\$ —	\$ —
\$9,290,100	First Mortgage 5% Bonds due 1946	—	14,787,000 (30%)	—	17,251,550 (35%)	17,251,550 (35%)
—	New Money from Reconstruction Finance Corporation	—	—	10,000,000	—	—
2,963,000	Notes held by Reconstruction Finance Corporation (June 30, 1935)	—	888,900 (30%)	—	1,037,050 (35%)	1,037,050 (35%)
4,999,800	Notes held by A. C. James Co.	—	—	—	—	—
2,538,956	Notes held by The Railroad Credit Corporation (June 30, 1935)	—	—	—	—	—
62,785,921	Total of Above Debt	—	—	—	—	—
28,300,000	Preferred 6% Stock	—	—	—	—	—
47,500,000	Common Stock	—	—	—	—	—
75,800,000	Total Stock	—	—	—	—	—
<b>Other Capital Liabilities</b>						
2,464,506	Interest due in 1934 on present Bonds	—	—	—	1,232,253 (50%)	1,232,253 (50%)
119,152	Interest due in 1934 on Notes to Reconstruction Finance Corporation	—	—	—	59,576 (50%)	59,576 (50%)
249,990	Interest due in 1934 on Notes to A. C. James Co.	—	—	—	—	—
29,385	Interest due in 1934 on Notes to The Railroad Credit Corporation	—	—	—	—	—
5,739,722	Principal due The Western Pacific Railroad Corp. (March 22, 1935)	—	—	—	—	—
51,667	Principal due The Western Realty Company	—	—	—	—	—
8,654,422	Total Other Capital Liabilities	—	—	—	—	—
\$147,240,343	Grand Total Capitalization	\$2,994,065	\$15,675,900	\$10,300,000	\$19,580,429	\$19,580,429







# CAPITALIZATION

Description	Present Capitalization	Proposed Assuming No Conversion Series "B" Bonds	Proposed Assuming Conversion All Series "B" Bonds
Equipment Trusts and Baldwin Lease	\$ 2,994,065	\$ 2,994,065	\$ 2,994,065
First Mortgage Debt	49,290,100	25,675,900	25,675,900
Total	52,284,165	28,669,965	28,669,965
R. F. C.-A. C. James Co.-R. C. C. Secured Debt	10,501,756	—	—
Total Fixed Interest Debt	62,785,921	28,669,965	28,669,965
Advances and Deferred Interest	8,654,422	—	—
Income Mortgage Bonds (Note 2)	—	39,160,858	19,580,429
Junior Lien Income Bonds	—	7,818,131	7,818,131
Total Debt	71,440,343	75,648,954	56,068,525
Preferred Stock—(Note 4)	28,300,000	—	—
Common Stock—(Note 4)	47,500,000 (Par \$100)	300,000 sh. (No Par)	887,412 sh. (No Par)
Total Stock	75,800,000	300,000 sh.	887,412 sh.
Total Capitalization	\$147,240,343	\$ 75,648,954 plus 300,000 sh.	\$ 56,068,525 plus 887,412 sh.
Approximate Interstate Commerce Commission valuation of The Western Pacific RR. Co. and owned subsidiaries	\$143,500,000	\$146,000,000	\$146,000,000

## ANNUAL BOND INTEREST REQUIREMENTS

Debt	On Present Bonds, Notes and Advances	Proposed Assuming No Conversion Series "B" Bonds	Proposed Assuming Conversion All Series "B" Bonds
Present Fixed Interest Debt	\$3,177,302	\$ —	\$ —
New First Mortgage Bonds (Note 5)	—	1,027,036	1,027,036
Contingent Mortgage Bonds—Series "A"	—	1,076,924	1,076,924
Contingent Mortgage Bonds—Series "B"	—	1,076,924	—
Junior Lien Bonds	—	469,087	469,087
Total (Note 5)	\$3,177,302	\$3,649,971	\$2,573,047

## NOTES

9a

### Note 1—Bonds to Be Purchased by Reconstruction Finance Corporation:

- (a) Reconstruction Finance Corporation is undertaking, subject to approval of the Interstate Commerce Commission, to (1) provide money for rehabilitation up to \$10,000,000 by the purchase of 30-year bonds to bear interest at 4% for the first ten years and at such higher rate thereafter as will make an average yield of 4½% from the date money is advanced to the maturity of bonds, or (2) in the alternative, to advance \$10,000,000 for twenty or twenty-five years at 4% collaterally secured by 120% of First Mortgage 4% Bonds.
- (b) Money will be drawn down over period of about 3 years as required to finance program of work.

### Note 2—Income Mortgage Bonds:

- (a) Income Mortgage Bonds to be issued in two series, viz:

#### Approximately

\$19,580,429	Series "A" 5½% Non-Convertible 50-Year Bonds.
19,580,429	Series "B" 5½% 50-Year Bonds convertible into 30 shares of no par value common stock for each \$1,000 bond.

- (b) Interest to be cumulative against two years' income.

### Note 3—Junior Lien Bonds:

tion No. 1

Junior Lien Income Bonds to be non-cumulative as to interest.

### Note 4—Common Stock:

- (a) Present Preferred and Common Stocks are \$100 par value.
- (b) Common Stock to have no par value and to be carried at stated value acceptable to Interstate Commerce Commission.

- (c) 300,000 shares to be issued on consummation of plan.

- (d) 587,412 shares to be reserved for conversion of Series "B" Income Bonds at rate of 30 shares for each \$1,000 bond.

- (e) As to the 300,000 shares of common stock allocated to the present equity, 150,000 shares to be placed in escrow and in any one year, after a five-year period that full interest is not paid on all of the income mortgage bonds, shares from this 150,000 to be given to the bondholders in the ratio of two shares of common stock for each full interest coupon. Unless there is a reduction for the foregoing reasons in the amount of common stock allocated to the equity (300,000 shares), the present equity would be entitled to any dividends declared on the 300,000 shares.

### Note 5—Annual Interest Under Plan:

Annual requirements shown include interest at 4% on full \$10,000,000 of bonds which may ultimately be sold to the Reconstruction Finance Corporation. Under circumstances indicated in Note 1(a), this interest rate would be increased after first ten years.

### Note 6—Interest Fund:

An interest fund is to be created into which shall be paid a minimum of 10% of net earnings available for the common stock until the fund equals one year's interest on fixed and contingent interest debt. Fund to be invested in Government Bonds.

### Note 7—Financial Control:

Provision to be made satisfactory to First Mortgage Bondholders, assuring them financial control of the reorganized company through representation on the Board of Directors and Executive Committee.

[Endorsed]: Filed Aug. 2, 1935.





[Title of District Court and Cause.]

ORDER

Upon due consideration of the petition of The Western Pacific Railroad Company, the above named debtor, verified August 2, 1935, and filed herein this day, stating that such debtor is unable to meet its debts as they mature and that it desires to effect a Plan of Reorganization in accordance with Section 77 of Chapter VIII of the Acts of Congress relating to bankruptcy, and the Court being satisfied that such petition complies with said section and has been filed in good faith, it is Ordered:

(1) That said petition be, and hereby is, approved as properly filed under Section 77 of Chapter VIII of the Acts of Congress relating to bankruptcy.

(2) That the debtor be, and it hereby is, authorized and directed, pending further order of the court in the premises, to run, manage, maintain, operate and keep in proper condition and repair the railroads and property of the debtor, wherever situated, whether in this state, judicial circuit, or elsewhere and to manage and conduct its business as a railroad company, and to this end to exercise its authority and franchises and discharge all public duties obligatory upon it, and to employ and discharge and fix the compensation of all officers, attorneys, managers, superintendents, agents and employees; to collect and [6] receive the incomes, rents, révenues, tolls, issues and profits of said



property; to collect all outstanding accounts and all dividends and interest on securities belonging to it; to exercise such sale, conveyance, exchange and release rights as are reserved to, or available to, the debtor, under outstanding deeds of trust, mortgages, trust indentures and similar instruments, and to use the proceeds of sale of all released property as provided in such instruments; all in the same manner that it would be entitled and bound to do in its own right; and, to the extent necessary to protect and preserve the property of the debtor, to make and pay for additions and betterments to the railroads and property of the debtor; and to make such advances to its subsidiary corporations as are necessary to protect the debtor's interest therein, all in the same manner that it would be entitled and bound to do in its own right; and, to the extent necessary to protect and preserve the property of the debtor, to make and pay for additions and betterments to the railroads and property of the debtor, all of the foregoing powers to be exercised according to law, and subject to such supervision and control by the Court as the Court may exercise by further orders entered herein. The authority given by the foregoing shall not include authority to incur expense, other than such as is necessary in the course of the usual and ordinary maintenance and operation of the debtor's property. Any extraordinary expense and expense incident to the reorganization of the debtor shall be subject to the prior approval of the Court.

(3) That the debtor is authorized, in its discretion from time to time until further order of this Court, out of funds now or hereafter coming into its hands, to pay:

(a) All taxes and assessments due or to become due upon the property of the debtor.

(b) All necessary expenses of operating the railroads and conducting the business of the debtor, including among other expenses the wages, salaries and compensation of all officers, attorneys, counsel, managers, superintendents, agents and employees retained by the [7] debtor; ticket, traffic, car mileage and car per diem balances; interline accounts; freight and overcharge claims; interest on and installments of principal of equipment trust obligations; and amounts for car and equipment repairs now due or that may become due to connecting or other railroad companies or other common carriers, including all sums now due or which may hereafter become due to other persons or corporations for the occupation or use, jointly or otherwise, of buildings, depots, terminals, tracks, side tracks, yards, warehouses, shops, bridges and other railroad facilities, and such sums as may be necessary to comply with the obligations of the debtor under contracts by virtue of which said occupation or use may now or hereafter be enjoyed (but such payments shall not constitute affirmations of said contracts, or of any of them):

(c) The following claims incurred by the debtor within six months preceding the date of this order, in the usual and customary operation of its properties, and the conduct of its current business, to-wit: Wages, salaries, fees, and other charges due and payable for services rendered to the debtor, unpaid material and supply accounts incurred in the operation of said properties; unpaid and outstanding pay checks and wage checks representing labor actually performed for the debtor. The debtor is also authorized in its discretion to adjust, compromise and pay claims of shippers, consignees, or others in interest, for overcharges or reparation awards; and for loss, damage or delay to freight and baggage; also to settle and pay on behalf of itself and other carriers and private car owners, claims arising out of rate [8] divisions, interline settlements, per diem accounts, switching reclaims, proportion of reparation awards, and freight charges or adjustments respecting shipments with transit or storage privileges and other charges or adjustments of like character, between carriers in the conduct of their joint business, regardless of when accrued.

(d) Pending further order of this Court in the premises, the debtor hereby is authorized to pay pay checks, and like instruments issued to employees for services rendered to the debtor, whether before or during said six months.

period, whenever the same are presented for payment.

(e) The cost of maintaining the corporate existence of the debtor, including the necessary expenses of the preservation of records, and the registration and transfer of its stocks and bonds, and trustees' charges under indenture under which securities of the debtor have been issued.

(f) All monthly payments due from time to time under any existing pension or insurance system of the debtor.

(g) The expense of printing pleadings, motions, petitions and orders now on file or hereafter filed in this case reasonably necessary to be printed, in such quantity as shall provide copies for the use of the Court, the debtor, parties to the cause, and such others as may have a substantial interest therein: such expense to be taxed as costs in this case.

(4) That the debtor shall be allowed until January 1, 1936 (unless the time be extended further by order of this Court), within which to disaffirm any contracts. Such disaffirmance shall be indicated by notice to that effect, in writing, served on the [9] other party or parties to such contract, and filed of record in this proceeding, and continued operation by the debtor under any of said contracts, within said period allowed for disaffirmances, shall not be deemed to conclude the debtor in respect of such election, or to constitute an election.

(5) That, pending further order of the Court in the premises, the debtor is authorized and empowered to institute or prosecute in any Court, or before any tribunal of competent jurisdiction, all such suits and proceedings as may be necessary, in its judgment, for the recovery or proper protection of its property or rights, and to make settlement of any thereof; and likewise to defend or liquidate, by written agreement or consent judgments, any actions, claims, proceedings, or suits, now pending against the debtor, or which may hereafter be asserted, or be brought in any Court, or before any officer, department, commission or tribunal, to which the debtor is, or shall be, a party, but no payments shall be made by the debtor in respect of any such claims accruing prior to the date of this order, in respect of any actions, proceedings, or suits, or such claims, without further order or direction of this Court except as may be provided in other paragraphs of this order and except such as may be permitted by other general orders hereafter entered herein, and such as constitute preferred claims under the Acts of Congress relating to bankruptcy; and no action taken by the debtor in defense or settlement of such claims, actions, proceedings, or suits, shall have the effect of establishing any claim upon, or right in, the property or funds in the possession of the debtor, that otherwise would not exist.

(6) That the debtor shall close its present books of account as of the close of business on July 31, 1935. The debtor shall open new books of account as of the opening of business on August 1, 1935.



and cause to be kept therein due and proper [10] accounts of the earnings, expenses, receipts and disbursements of the debtor, and shall preserve proper vouchers for all payments made on account thereof, and shall deposit the moneys coming into its hands in such of the banks in which funds of the debtor are presently deposited as shall be selected by the debtor, or in such other bank or banks as shall be selected by and approved by this Court.

(7) That within sixty days after the entry of this order, the debtor shall file with the Clerk of this Court a statement of the assets and liabilities of the debtor as of the close of business on July 31, 1935, and within fifty days after the close of each calendar month thereafter shall file with said Clerk a statement of the assets and liabilities of the debtor as of the close of business on the last day of the second preceding calendar month, together with a summary statement of the revenues and expenses of the debtor of the second preceding calendar month. All such statements shall be certified as correct by the chief accounting officer of the debtor.

(8) That all persons, firms and corporations, whatsoever and wheresoever situated, located, or domiciled, hereby are restrained and enjoined from interfering with, attaching, garnisheeing, levying upon, and enforcing liens upon, or in any manner whatsoever disturbing any portion of the assets, goods, money, railroads, properties and premises belonging to, or in the possession of the debtor, or from taking possession of the same, or any part.



thereof, or in any way interfering in any manner to prevent the discharge by the debtor of its duties in the operation of said property and business, under the orders of this Court, or from bringing any new suits or actions, accruing prior to this date, in or before any Court from which an appeal or proceedings to review, can be taken only upon the filing of an appeal bond, as a jurisdiction or mandatory requirement. [11]

(9) That all persons and corporations holding collateral heretofore pledged by the debtor as security for its notes or obligations be, and each of them is, hereby restrained and enjoined from selling, converting or otherwise disposing of such collateral, or any part thereof, until further order of this Court.

(10) This Court reserves full power and jurisdiction to make from time to time such orders amplifying, extending, limiting or otherwise modifying this order as to the Court may at any time seem proper.

(Sgd) A. F. ST. SURE  
District Judge

Dated: August 2, 1935.

[Endorsed]: Filed Aug. 2, 1935. [12]

The Western Pacific Railroad Company

---

**PLAN OF REORGANIZATION**

Effective date January 1, 1936

---

Presented by  
The Western Pacific Railroad Company pursuant to  
Section 77 of the Bankruptcy Act.

[119]

The Western Pacific Railroad Company  
Office of Chairman of the Executive Committee  
37 Wall Street,  
New York

T. M. Schumacher,  
Chairman.

— In the Matter of the Reorganization  
of  
The Western Pacific Railroad Company

---

FEBRUARY 7, 1936.

To:

The Honorable, the District Court of the United  
States for the Northern District of California,  
Southern Division, and

The Honorable, the Interstate Commerce Commis-  
sion, Washington, D. C.

There is annexed hereto for filing pursuant to  
sub-section (d) of § 77 of the Bankruptcy Act,

the Plan of Reorganization of The Western Pacific Railroad Company, an outline of which was submitted as part of this Company's petition filed under said Act on August 2, 1935.

This plan of Reorganization prepared as the result of conferences with the Committee of Bondholders referred to therein and with Reconstruction Finance Corporation and other creditors will be presented by this Company at the public hearing heretofore requested by it under said Section 77.

THE WESTERN PACIFIC  
RAILROAD COMPANY.

By T. M. SCHUMACHER,

Chairman of the Executive Committee

[120]

The Western Pacific Railroad Company  
(hereinafter called the Railroad Company)

---

PLAN OF REORGANIZATION

Effective Date January 1, 1936

---

I.

Procedure

As the means for the execution of the plan with a minimum of delay and expense it is proposed to continue the Railroad Company, with any necessary or appropriate amendments to its Articles of Incorporation and By-Laws, but the right is reserved to create a new Company or to resort to any

procedural methods sanctioned by Section 77 of the Bankruptcy Act, or any amendment thereof, for the issuance of the new securities in substitution for those to be retired under the Plan, and for the protection of any class of creditors or stockholders who may not accept the Plan.

## II.

### Summary of the Plan

For convenient reference a tabulated summary of the Plan showing the bases of conversion of present securities of the Railroad Company into securities of the reorganized Company appears on the following page. A detailed statement respecting each of the proposed new securities and the terms of issue appears at a subsequent point.

The underlying purpose of the Plan is the creation of a revised capital structure providing for fixed charges believed to be within the probable prospective earnings of the reorganized Company under any conditions reasonably to be expected in the future; also to provide funds for necessary rehabilitation work including deferred maintenance which necessarily accrued during the depression period. *Fixed annual interest is to be reduced from \$3,180,053 to \$1,027,036,\** including in the latter figure interest at 4% on \$10,000,000, the maximum of new money to be provided by Reconstruction Finance Corporation. [121]

---

\* Italics used throughout this paper were used in the original document.



**THE WESTERN PACIFIC RAILROAD COMPANY**  
**SUMMARY OF PLAN OF REORGANIZATION**  
(Effective Date January 1, 1936)

Existing Capitalization and Other Capital Liabilities			Proposed Capitalization						
Amount and Nature of Obligation (December 31, 1935)		Equipments to be Undisturbed	Fixed 4% First Mortgage 30-Year Bonds	Fixed 4-1/2% First Mortgage 30-Year Bonds	Series "A" 5 1/2% Income Mortgage 50-Year Sinking Fund Bonds	Series "B" 5 1/2% Income Mortgage 50-Year Convertible Bonds	Junior Lien 6% Income 75-Year Bonds	New No-Par Common Stock	Proposed Total
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)
<b>Existing Capitalization</b>									
\$ 2,682,598	Equipment Trusts and Baldwin Lease	\$2,682,598	\$ —	\$ —	\$ —	\$ —	\$ —	—	\$ 2,682,598
(A) 49,299,100	First Mortgage 5% Bonds, due 1946	—	14,787,000 (30%)	—	17,251,550 (35%)	17,251,550 (35%)	—	—	49,299,100
—	New Money to be provided by Reconstruction Finance Corporation	—	—	10,000,000	—	—	—	—	10,000,000
(B) 2,963,000	Notes—Reconstruction Finance Corp.	—	888,900 (30%)	—	1,037,050 (35%)	1,037,050 (35%)	—	—	2,963,000
(B) 4,999,800	Notes—A. C. James Co.	—	—	—	—	—	4,999,800	—	4,999,800
(B) 2,524,907	Notes—The Railroad Credit Corp.	—	—	—	—	—	2,524,907	—	2,524,907
\$ 62,460,405	Total of above debt	—	—	—	—	—	—	—	—
28,300,000	Preferred 6% Stock—Par \$100+	—	—	—	—	—	—	—	—
47,500,000	Common Stock—Par \$100	—	—	—	—	—	—	300,000 Sh.	390,000 Sh.
\$ 75,800,000	Total Stock	—	—	—	—	—	—	—	—
<b>Other Capital Liabilities</b>									
\$ 4,928,760	Matured First Mortgage Bond Interest Unpaid	—	—	—	2,464,380	2,464,380	—	—	4,928,760
268,836	Matured Interest Unpaid—Reconstruction Finance Corporation	—	—	—	134,418	134,418	—	—	268,836
499,980	Matured Interest Unpaid—A. C. James Co.	—	—	—	—	—	499,980	—	499,980
68,022	Matured Interest Unpaid—The Railroad Credit Corporation	—	—	—	—	—	68,022	—	68,022
6,897,274	Principal and accrued interest due The Western Pacific Railroad Corp.†	—	—	—	—	—	—	—	—
54,167	Principal and accrued interest due The Western Realty Company†	—	—	—	—	—	—	—	—
\$ 12,717,039	Total Other Capital Liabilities	—	—	—	—	—	—	—	—
\$150,977,444	Grand Total	\$2,682,598	\$15,675,900	\$10,000,000	\$20,887,398	\$20,887,398	\$8,092,709	300,000 Sh.	\$78,226,063 plus 300,000 Sh.

(A)—The First Mortgage Bonds are outstanding under an indenture dated June 26, 1916 executed by the Railroad Company to First Federal Trust Company (now

(Effective Date January 1, 1935)

## Existing Capitalization and Other Capital Liabilities

## Proposed Capitalization

Amount and Nature of Obligation (December 31, 1935)		Equipment to be Undisturbed	Fixed 4% First Mortgage 30-Year Bonds	Fixed 4-1/2% First Mortgage 30-Year Bonds	Series "A" 5 1/2% Income Mortgage 50-Year Sinking Fund Bonds	Series "B" 5 1/2% Income Mortgage 50-Year Convertible Bonds	Junior Lien 6% Income 75-Year Bonds	New No Par Common Stock	Proposed Total
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)
Existing Capitalization									
\$ 2,682,598	Equipment Trusts and Baldwin Lease	\$2,682,598	\$ —	\$ —	\$ —	\$ —	\$ —	—	\$ 2,682,598
(A) 49,290,100	First Mortgage 5% Bonds, due 1946	—	14,787,000 (30%)	—	17,251,550 (35%)	17,251,550 (35%)	—	—	49,290,100
—	New Money to be provided by Reconstruction Finance Corporation	—	—	10,000,000	—	—	—	—	10,000,000
(B) 2,963,000	Notes—Reconstruction Finance Corp.	—	888,900 (30%)	—	1,037,050 (35%)	1,037,050 (35%)	—	—	2,963,000
(B) 4,999,800	Notes—A. C. James Co.	—	—	—	—	—	4,999,800	—	4,999,800
(B) 2,524,907	Notes—The Railroad Credit Corp.	—	—	—	—	—	2,524,907	—	2,524,907
\$ 62,480,405	Total of above debt.	—	—	—	—	—	—	—	—
28,300,000	Preferred 6% Stock—Par \$100	—	—	—	—	—	—	—	—
47,500,000	Common Stock—Par \$100	—	—	—	—	—	—	300,000 Sh.	300,000 Sh.
\$ 75,800,000	Total Stock	—	—	—	—	—	—	—	—
Other Capital Liabilities									
\$ 4,928,760	Matured First Mortgage Bond Interest Unpaid	—	—	—	2,464,380	2,464,380	—	—	4,928,760
268,836	Matured Interest Unpaid—Reconstruction Finance Corporation	—	—	—	134,418	134,418	—	—	268,836
499,980	Matured Interest Unpaid—A. C. James Co.	—	—	—	—	—	499,980	—	499,980
68,022	Matured Interest Unpaid—The Railroad Credit Corporation	—	—	—	—	—	68,022	—	68,022
6,897,274	Principal and accrued interest due The Western Pacific Railroad Corp.	—	—	—	—	—	—	—	—
54,167	Principal and accrued interest due The Western Realty Company	—	—	—	—	—	—	—	—
\$ 12,717,939	Total Other Capital Liabilities	—	—	—	—	—	—	—	—
\$150,977,444	Grand Total	\$2,682,598	\$15,675,900	\$10,000,000	\$30,887,398	\$20,887,398	\$8,092,709	300,000 Sh.	\$78,226,003 plus 300,000 Sh.

(A) The First Mortgage Bonds are outstanding under an indenture dated June 26, 1916 executed by the Railroad Company to First Federal Trust Company (now Crocker First National Bank of San Francisco) and Henry E. Cooper, Trustees. Samuel Armstrong was substituted as Co-trustee in place of Henry E. Cooper, effective January 28, 1935.

(B) The Railroad Company has issued as collateral for notes held by Reconstruction Finance Corporation, The Railroad Credit Corporation and A. C. James Co., \$18,999,500 of General and Refunding Mortgage Bonds which are to be cancelled under the Plan. These Bonds are issued under an indenture dated January 1, 1932 executed by the Railroad Company to The Chase National Bank of the City of New York, Trustee.

(C) Cancelled under the Plan.





The tabulation on the opposite page shows in Column 1 the present outstanding securities and other Capital Liabilities, and, in Columns 3 to 9, inclusive, what the holders of present securities would receive under the Plan.

As appears in Columns 4, 6 and 7, holders of present First Mortgage ~~5%~~ Bonds are to receive new fixed interest. First Mortgage 4% Bonds to the extent of 30% of the face value of their present holdings and 35% in Series "A" and 35% in Series "B" Income Bonds on which interest at  $5\frac{1}{2}\%$  will be payable to the extent earned as more fully set forth in Article V of this Plan, and, in addition, Series "A" and Series "B" bonds in equal proportions of face value equal to the full amount of unpaid 1934 and 1935 interest. Series "A" and Series "B" bonds are to be the same in all respects except that Series "A" are to be subject to a Sinking Fund and Series "B" are to be convertible, under certain conditions in said Article V stated, into Common Stock.

The proposed treatment of other secured and unsecured debt is similarly indicated.

All of the Common and Preferred Stock of The Western Pacific Railroad Company is owned by The Western Pacific Railroad Corporation, a holding company, and treatment of the Corporation's stock ownership is also shown by the tabulation.

In Article III, which immediately follows, will be found tabulations showing comparisons in convenient form of present and proposed debt structure and present and proposed interest requirements. [123]



## III.

## Comparisons

As showing that the Plan will be financially advisable and compatible with the public interest, the following comparisons are submitted:

(1)

## COMPARISON OF PRESENT AND PROPOSED CAPITALIZATIONS

Description	Present	Proposed Capitalization	
	Capitalization Dec. 31, 1935	Assuming No Conversion Series "B" Bonds	Assuming Conversion All Series "B" Bonds
(1)	(2)	(3)	(4)
Equipment Trusts and Baldwin Lease	\$ 2,682,598	\$ 2,682,598	\$ 2,682,598
First Mortgage Bonds	49,290,100	25,675,900	25,675,900
Total	51,972,698	28,358,498	28,358,498
R' F. C.—A. C. James Co.—R. C. C. Secured Debt	10,487,707	—	—
Total Fixed Interest Debt	62,460,405	28,358,498	28,358,498
Other Capital Liabilities—Principal and Unpaid Interest	12,717,039	—	—
Income Mortgage Bonds—Series "A"	—	20,887,398	20,887,398
Income Mortgage Bonds—Series "B"	—	20,887,398	—
Junior Lien Income Bonds	—	8,092,709	8,092,709
Total Debt	75,177,444	78,226,003	57,338,605
Preferred Stock	28,300,000	—	—
Common Stock	47,500,000 (Par \$100)	300,000 Sh. (No Par)	926,622 Sh. (No Par)
Grand Total	\$159,977,444	\$ 78,226,003 plus 300,000 Sh.	\$ 57,338,605 plus 926,622 Sh.

Note: Present value, on an Interstate Commerce Commission basis, of The Western Pacific Railroad Company and final or tentative values of owned subsidiaries totals approximately \$143,500,000. Estimated capital expenditures incident to the rehabilitation program, for which new money is to be obtained, will increase this value to approximately \$146,500,000.

(2)

COMPARISON OF PRESENT FIXED ANNUAL INTEREST REQUIREMENTS WITH PROPOSED  
FIXED INTEREST REQUIREMENTS AND INTEREST PAYABLE ONLY IF EARNED.

Item of Debt (1)	On Present	Proposed	
	Debt Structure (2)	Assuming No Conversion Series "B" Bonds (3)	Assuming Conversion All Series "B" Bonds (4)
Fixed Annual Interest:			
First Mortgage Bonds	\$2,464,505	\$ —	\$ —
Other Funded and Unfunded Debt (1935)	715,548	—	—
New First Mortgage Bonds at 4% (See Note A)	—	1,027,036	1,027,036
Total	\$3,180,053	\$1,027,036	\$1,027,036
Equipment Trusts and Baldwin Lease (1936) (See Note B)	121,681	121,681	121,681
Interest Payable Only if Earned:			
Income Mortgage Bonds, Series "A" at 5 1/2%	—	1,148,806	1,148,806
Income Mortgage Bonds, Series "B" at 5 1/2%	—	1,148,806	—
Junior Lien Income Bonds at 6%	—	485,563	485,563
Total Payable if Earned	\$ —	\$2,783,175	\$1,634,369
Grand Total	\$3,301,734	\$3,811,892	\$2,783,086

Note A: Proceeds from sale of bonds to Reconstruction Finance Corporation within the maximum of \$10,000,000 will be drawn down over a period of about three years as required to finance the program of rehabilitation and for a Contingency Reserve Fund. Interest is shown above on maximum amount of such bonds at the rate of 4% which will prevail for first ten years.

Note B: Equipment Trust principal in the amount of \$2,682,598 is reduced annually with corresponding decrease in annual interest.





## IV.

## New Money From Reconstruction Finance Corporation

An outstanding feature of the Plan is the undertaking of Reconstruction Finance Corporation, subject to approval and authorization of the Interstate Commerce Commission, to provide money for rehabilitation and working capital up to \$10,000,000 by the purchase at par of new Thirty-year First Mortgage Bonds which may bear interest at 4% for the first ten years and at such higher rate or rates thereafter as will make an average yield of  $4\frac{1}{2}\%$  from the date the money is advanced to the maturity of the Bonds.

The right, however, is reserved (a) to issue these bonds bearing a 4% interest rate to maturity and to adjust the additional  $1\frac{1}{2}\%$  in the purchase price of the Bonds, or (b) to accept an alternative proposal to advance \$10,000,000 for 20 or 25 years at 4% collaterally secured by 120% of First Mortgage Bonds of the reorganized Company.

All Bonds issuable on this account may be authenticated forthwith and placed in the treasury of the reorganized Company. They shall be issued against the surplus created as a result of the reorganization, and their proceeds shall be available for such capital and rehabilitation expenditures as the Board of Directors, after providing for a Contingency Reserve Fund, may deem proper. All re-

habilitation expenditures other than those chargeable to Capital Account shall be charged to surplus, and the necessary authorization of such charges by the Interstate Commerce Commission is a part of this Plan. Out of the proceeds of such Bonds there shall be set apart \$500,000, as a Contingency Reserve Fund, which shall be available only for the purpose of paying fixed interest charges, principal of and dividends on Equipment Trust obligations and operating expenses which cannot otherwise be provided for without, in the opinion of the Board of Directors, unduly impairing free working capital. As such new Bonds are disposed of from time to time, the proceeds, except such part as may be so set apart, shall be placed in a special fund to be disbursed only to meet expenses of the rehabilitation and improvement or equipment [125] program except that such proceeds (a) may be used for such additions and betterments as the Board of Directors may substitute for any part of such program or authorize after its completion and (b) may be resorted to if necessary to avert a default under the Fixed 4% Mortgage or any Equipment Trust Agreement of the reorganized Company.

It is estimated that the work program will cover a period of not less than three years from January 1, 1936.

This undertaking to advance new money is made by Reconstruction Finance Corporation on condition that its existing claim against the Railroad Company amounting to \$2,963,000 represented by

collateral notes junior to the existing First Mortgage Bonds be refunded under the Plan in like securities and in like proportions as those given holders of existing First Mortgage Bonds.

V.

Description of New Securities

A First Mortgage Bonds:

The new First Mortgage shall constitute a first lien upon all the railroads and fixed property, real and personal, and equipment of the reorganized Company now pledged under the First Mortgage of the Railroad Company. The total authorized issue of Bonds thereunder is to be limited to \$50,000,000, of which

\$15,675,900 are to be distributed under the Plan;

10,000,000 are to be purchased by or used in part to collateralize loans from Reconstruction Finance Corporation,

1,000,000 are to be issued forthwith and placed in the Treasury of the reorganized Company free from restriction; and

23,324,100 are to be reserved to be issued to provide for, or to reimburse the reorganized Company for expenditures made for additions, betterments, [126] improvements or extensions, in a principal amount not exceeding 75% of the actual cost of such additions, betterments, improvements or extensions. If the Board of Directors of

the reorganized Company shall elect to accept the alternative proposal of Reconstruction Finance Corporation described in clause (b) of the second paragraph of Article IV hereof, \$2,000,000 of the reserved Bonds may, however, be used as collateral to loans from Reconstruction Finance Corporation, but upon payment of such loans the further issue of said \$2,000,000 of reserved Bonds shall be subject to the limitations hereinbefore provided.

The First Mortgage Bonds may be issued in series which may differ as to date of maturity and interest rate but the Bonds immediately issuable under the Plan are to be dated January 1, 1936, are to mature January 1, 1966, and are to bear interest at 4% per annum, except that such of said Bonds as may be sold to Reconstruction Finance Corporation under the alternative proposal described in clause (a) of the second paragraph of Article IV hereof, may bear interest at varying rates not exceeding an average of 4½% from the date of issue to the date of maturity of the Bonds.

The First Mortgage Bonds to be distributed under the Plan and all First Mortgage Bonds sold or pledged to Reconstruction Finance Corporation shall be redeemable in whole or in part on any interest payment date, upon 30 days' notice, at their principal amount and accrued interest.



B. Income Mortgage 5½% Bonds:

1. The Income Mortgage will be a lien upon all of the railroads and property covered by the First Mortgage, subject only to the lien of the First Mortgage. The Bonds issued under the Income Mortgage are to be limited to [127]

\$20,887,398 Series "A" 5½% Income Mortgage  
50-Year Sinking Fund Bonds (hereinafter  
called the Series "A" Bonds), and

20,887,398 Series "B" 5½% Income Mortgage  
50-Year Convertible Bonds (hereinafter  
called the Series "B" Bonds).

All of the Series "A" Bonds and the Series "B" Bonds are immediately issuable under the Plan and are to be equally and ratably secured by the Income Mortgage.

The Series "A" Bonds are to be dated January 1, 1936, are to mature January 1, 1986, are to bear interest at the rate of 5½% annually, payable as provided in the Income Mortgage only out of Available Net Income, and are entitled to the benefit of a cumulative Sinking Fund not to exceed in any year one-half of 1% of the largest principal amount of such Bonds theretofore issued.

The Series "B" Bonds are to be dated January 1, 1936, are to mature January 1, 1986, are to bear interest at the rate of 5½% annually, payable as provided in the Income Mortgage only out of Available Net Income, are to be convertible into common stock of the reorganized Company at the rate of

thirty shares of such stock for each \$1,000 principal amount of such Bonds.

Income Bonds of both Series "A" and Series "B" are to be redeemable, in whole or in part, upon 30 days' notice, on any interest payment date, at their principal amount, together with any interest thereon payable on said date, payable out of Available Net Income for fixed charges as hereinafter provided.

As more fully provided in Section 3 of this subdivision B, interest on the Income Mortgage  $5\frac{1}{2}\%$  Bonds of both Series "A" and "B" shall be cumulative, as against the Available Net Income of the reorganized Company, for the Income Period in respect of which such interest is payable and for the four Income Periods next succeeding the Income Period in respect of which such interest is payable. If on any April 1 or [128] October 1, commencing April 1, 1941, full interest at the rate of  $5\frac{1}{2}\%$  per annum shall not be paid on the Series "A" and the Series "B" Income Mortgage Bonds in respect of the next preceding Income Period, there shall be delivered out of the escrow provided for in Article VI hereof to the holders of such Bonds, Common Stock of the reorganized Company (or Voting Trust Certificates therefor, so long as the Voting Trust hereinafter provided for shall continue) in respect of any deficiency in the payment of such full interest, at the price of \$27.50 per share. In respect of fractional shares becoming so deliverable, scrip will be issued, convertible into

Common Stock (or Voting Trust Certificates) in amounts aggregating full shares.

Any such stock remaining in escrow, when all Series "A" and Series "B" Bonds shall have been retired, shall be delivered to holders of Escrow Receipts covering such stock.

2. Available Net Income shall be determined for each period of six months ending June 30 or December 31 (hereinafter called Income Periods) beginning with the Income Period of the reorganized Company ending June 30, 1936. Available Net Income for any Income Period shall be determined by deducting from "income of the reorganized Company available for fixed charges" for such Income Period (determined in accordance with accounting rules of the Interstate Commerce Commission or other analogous Federal authority having jurisdiction in the premises, at the time in force):

(a) All fixed charges of the reorganized Company accrued during such Income Period; and

(b) All other charges properly deductible from such income in determining income after fixed charges (under such accounting rules then in force), but excluding contingent interest, or Sinking Fund requirements hereinafter provided for.

3. Available Net Income for each Income Period shall be applied to the following purposes and in the following order: [129]

(a) To the maintenance of the Contingency Reserve Fund at \$500,000. provided, however, that the amount applied to this purpose shall not exceed 10% of the Available Net Income for such Income Period.

(b) To the creation of a Capital Fund to be applied to or to provide for or reimburse the treasury of the reorganized Company for Capital Investments (as defined by the Interstate Commerce Commission Classification of Income, Profit and Loss and General Balance Sheet Accounts for Steam Roads, Accounts Nos. 701, 702, 705 and 706 then in effect and including therein initial and principal payments on equipment leased under equipment trusts or purchased under conditional sale agreements) to the extent that such Capital Investments have been made during such Income Period, provided, however, that (1) to the extent that expenditures are so provided for or reimbursed out of the Capital Fund, the reorganized Company shall not thereafter have the right to issue any Bonds or other evidence of indebtedness to capitalize or reimburse such expenditures; that (2) the amount set aside in the Capital Fund out of the Available Net Income of any calendar year shall not exceed \$500,000. during the years 1936 to 1940, both inclusive, \$1,000,000. during the years 1941 to 1945, both inclusive, and in all subsequent years not more than 3% of the gross revenues of the

reorganized Company for the next preceding calendar year and (3) that any unappropriated amount not charged out as of December 31 in any year shall not be carried forward.

(c) To the payment on April 1 and October 1 in each year of interest on the Series "A" Bonds and the Series "B" Bonds, above described accruing during the Income Period ending on the next preceding December 31 and June 30, respectively, and, to the extent unpaid, any interest which shall have accrued on [130] said Bonds in respect of four Income Periods next preceding such Income Period, all without preference in favor of either series as against the other.

(d) To the creation of a cumulative Sinking Fund in an amount not exceeding in any calendar year one-half of 1% of the largest principal amount of Series "A" Bonds theretofore issued. Said Sinking Fund shall be applied to the purchase of Income Bonds, Series "A", at not exceeding their redemption price; and whenever the amount in the Sinking Fund exceeds \$100,000 and Income Bonds, Series "A", are not tendered or cannot otherwise be purchased at less than their redemption price, the funds then in the Sinking Fund shall be applied to the redemption of Income Mortgage Bonds, Series "A", on the next succeeding interest payment date. Bonds purchased or redeemed out of the Sinking Fund shall not there-



after be-issuable, but the amount of interest which would otherwise have become payable thereon out of Available Net Income shall be added to the Sinking Fund on each April 1 and October 1 so long as any Income Bonds, Series "A" shall be outstanding.

(e) To the payment on April 1 and October 1 in each year of interest on the Junior Lien 6% Income Bonds.

(f) To the creation of an Interest Fund into which shall be paid from time to time 10% of the Available Net Income remaining after the payments provided for in the preceding clauses (a), (b), (c), (d) and (e), provided, however, that such payments shall not be required to be made into said Interest Fund from the Available Net Income of any Income Period at the end of which the amount of said Interest Fund shall aggregate at least one year's interest on all outstanding First Mortgage Bonds, including First Mortgage Bonds pledged as collateral for other obligations of the reorganized Company and 120% of such part of [131] the \$10,000,000 provided to be supplied by Reconstruction Finance Corporation which shall not have been supplied at the end of such Income Period. Said Interest Fund shall be available only for the payment of interest upon the First Mortgage Bonds, and, pending such application, shall be invested in such manner as the Board of Directors of

the reorganized Company may in its discretion determine. The obligation to make payments into and to maintain said Interest Fund shall cease whenever for five consecutive years the Net Income of the reorganized Company available for fixed charges shall have equalled three times the amount of such fixed charges, and full interest and Sinking Fund shall have been paid on, and for, the Income Mortgage Bonds.

(g) To general corporate purposes, including dividends on Common Stock.

4. Interest on Income Mortgage Bonds shall be paid only in amounts equal to one-fourth of 1%, or multiples thereof, smaller fractional amounts being carried forward and added to that portion of the Available Net Income for the next succeeding Income Period required to be applied to the payment of interest of such Bonds.

**C. Junior Lien 6% Income Bonds**

The Junior Lien Mortgage will be a lien upon all of the railroads and property covered by the First Mortgage, subject to the prior liens of the First Mortgage and the Income Mortgage.

The Bonds issued under and secured by the Junior Lien Mortgage are to be limited to \$8,092,709, all of which are issuable forthwith under the Plan.

The Junior Lien 6% Income Bonds are to be dated January 1, 1936, are to mature January 1, 2011, are to bear interest at the rate of 6% per annum payable as provided in the Junior Lien Mort-

page only out of Available Net Income, and are to be non-cumulative. [132]

D. Common Stock:

The Common Stock is to be without par value and is to be carried in the accounts of the reorganized Company at a value acceptable to the Interstate Commerce Commission. The authorized issue will be 926,622 shares, of which 300,000 will be issuable forthwith under the Plan and 626,622 will be reserved for issue upon conversion of \$20,887,398 Series "B" Bonds.

VI.

Participation of Bondholders in the Management of the Reorganized Company

The Board of Directors of the reorganized Company shall consist of seventeen members, a majority of which shall be citizens of the State of California.

For the protection primarily of the holders of the Income Bonds, all of the stock of the reorganized Company shall be placed in a Voting Trust under which three Voting Trustees nominated by the Railroad Company and approved by the Bondholders' Committee hereinafter mentioned at or before the hearing before the Interstate Commerce Commission upon this Plan shall act as Voting Trustees pursuant to a Voting Trust Agreement which shall be acceptable to the Railroad Company.

and the said Bondholders' Committee. Voting Trust Certificates shall be delivered in respect of Common Stock deposited under the Voting Trust Agreement. Such Voting Trust shall continue until ten years from the date upon which the Plan shall be finally confirmed by the Court. It is the intention of this provision and the Voting Trust Agreement shall provide that the reorganized Company shall during such period be managed by a board of directors, at least a majority of which shall in the opinion of the Voting Trustees be representatives of holders of Income Bonds. The Voting Trust Agreement shall also provide that, so long as Reconstruction Finance Corporation shall be the holder of more than \$500,000, principal amount, of First Mortgage Bonds or of notes of the reorganized Company secured by First Mortgage Bonds, the Voting [133] Trustees shall elect to the board of directors of the reorganized Company a person designated or nominated for that purpose by Reconstruction Finance Corporation. The Voting Trust Agreement shall provide that if any vacancy shall occur among the Voting Trustees, such vacancy shall be filled by a majority of the remaining Voting Trustees. Action of a majority of the persons at the time acting as Voting Trustees, at a meeting or in writing without a meeting, shall constitute the action of the Voting Trustees under the Voting Trust Agreement and under the Plan.

The reorganized Company shall, by By-law or otherwise, create a Finance Committee of not less

than three nor more than five members of its Board of Directors, of whom a majority shall be named from persons representing the Income Mortgage Bondholders, which Committee shall have supervision over all financial matters, including the annual budget of capital expenditures and all other expenditures of the reorganized Company's funds; and the reorganized Company shall covenant for the benefit of the Income Mortgage Bonds, to make only such expenditures as shall be authorized by said Finance Committee, exclusive of emergency expenditures and of capital items not exceeding \$25,000 for any item and not exceeding \$200,000 in the aggregate in any year.

The By-laws of the reorganized Company shall also provide for an Executive Committee having all the powers of the present Executive Committee of the Railroad Company, except as they may be vested in a Finance Committee as hereinbefore provided.

In respect of the 300,000 shares of Common Stock to be presently issued under the Plan and of any shares of Common Stock which may be issued on conversion of the Income Mortgage Bonds, Series "B", so long as the Voting Trust Agreement shall be in effect, Voting Trust Certificates shall be issued in such form as shall be provided in the Voting Trust Agreement.

Voting Trust Certificates for 150,000 shares of Common Stock shall be placed in escrow with the Trustee of the Income Mortgage for delivery to the



holders of the Income Mortgage Bonds in respect of interest deficiencies, as provided in paragraph 1 of subdivision B of Article V hereof, and to the extent that such delivery is not required prior to payment or retirement of all Income Mortgage Bonds of both Series "A" and Series "B", for delivery, upon [134] such payment or retirement, to holders of Escrow Receipts therefor, which shall be delivered to present holders of the Common Stock of the Railroad Company in lieu of said 150,000 shares of Common Stock (or Voting Trust Certificates therefor).

## VII.

### Method of Participation in and Consummation of the Plan

No holder of any security of the Railroad Company affected by the Plan shall be requested to accept the Plan until after a public hearing upon the Plan, held as provided in Section 77 of the Bankruptcy Act as it now exists or hereafter may be amended, and a report and order of the Interstate Commerce Commission approving the Plan, (in its present form or as it may be modified as hereinafter provided) and after the filing of an opinion and order of the Court approving the Plan and finding that the Plan complies with such Section 77. If and when the Interstate Commerce Commission and the Court shall so approve the Plan (including any modification thereof), such Plan shall be submitted in such manner as the Interstate Commerce

Commission shall direct to the security holders affected thereby for acceptance or rejection.

The Plan shall not be declared operative or carried out until finally approved by the Interstate Commerce Commission and confirmed by the Court after acceptance by the holders of such amount of each class or classes of securities or claims affected by the Plan as shall be sufficient under the provisions of the Bankruptcy Act as now existing or as it may hereafter be amended, to make the Plan binding upon the holders of all classes of securities or claims affected thereby.

The Board of Directors of the Railroad Company may, whether before or after its acceptance by holders of securities, modify the Plan or adopt a Substitute Plan in accordance with and subject to the provisions of Section 77 of the Bankruptcy Act as now existing or as it may hereafter be amended; and the term Plan as used herein shall be deemed to include any such modification or substitute Plan. [135]

Messrs. Frederick H. Ecker, John W. Stedman and Reeve Schley have heretofore acted as a Committee to represent certain large institutional holders of First Mortgage Bonds, being not more than twenty-five *bona-fide* holders thereof, in respect of the extension of the interest maturing during 1934 upon such First Mortgage Bonds, in respect of the performance of the Railroad Company's agreements made in connection with said extension and in the

negotiation of this Plan with the Railroad Company. Said Committee shall continue as a Committee to represent the interest of such holders of the present First Mortgage Bonds in connection with the reorganization, but assumes no representation of any other holders of said Bonds, and shall not represent holders of Income Bonds in the selection of directors for the reorganized Company. The members of such Committee have agreed to serve without commission, but the expenses of said Committee shall be reimbursed as hereinafter provided.

All acceptances or assents to the Plan shall be subject to the condition that the Plan shall have been finally confirmed by the Court, pursuant to Section 77 of the Bankruptcy Act. The Plan may be made effective retroactively to midnight on December 31, 1935, by the terms of the decree of confirmation, or on such later date as may, with the approval of the Interstate Commerce Commission, be fixed by agreement between (1) the Railroad Company, (2) Reconstruction Finance Corporation, and (3) Messrs. Frederick H. Ecker, John W. Stedman and Reeve Schley or their successors as such Committee.

The Board of Directors of the Railroad Company shall have power, subject to the provisions of the Plan and to the approval of said Committee or of their counsel, to determine the form and provisions of the several indentures, bonds, stock certificates, acceptances, assents, and other instruments in connection with carrying out the Plan.

All securities may be issued as of January 1, 1936, notwithstanding that confirmation of the Plan may be delayed beyond that date, and the base figures as set forth in the Plan may be adjusted to any effective date which may be substituted for January 1, 1936. Expenditures made for the rehabilitation program subsequent to January 1, 1936, but prior to confirmation of the [136] Plan, whether made out of current funds or from the proceeds of Trustees' Certificates, shall be reimbursed out of the proceeds of sale of the Fixed 4% First Mortgage Bonds purchased by Reconstruction Finance Corporation.

Unless otherwise provided in Section 77 of the Bankruptcy Act or in any order or orders of the Court or the Interstate Commerce Commission, whenever notice shall be required or permitted to be given under or pursuant to the Plan, such notice shall be given by publishing a copy of such notice once in each week in one newspaper published and of general circulation in the Borough of Manhattan, the City and State of New York, and in one newspaper published and of general circulation in the City of San Francisco, State of California, and also (1) in case of notices to security holders or creditors who have accepted the Plan, by mailing such notice, postage prepaid, to the addresses of such security holders or creditors set forth in the acceptances signed by them; and (2) in case of notices to security holders or creditors who shall not have accepted the Plan, by mailing such notice, postage prepaid,

to such security holders, or creditors whose names and addresses appear on the books of the Railroad Company.

All powers conferred by the Plan upon the Board of Directors of the Railroad Company may also be exercised by its Executive Committee.

### VIII.

#### Provision for Other Claims

The following claims are not affected by the Plan:

(a) current liabilities of the Railroad Company incurred in the ordinary conduct of its business prior to the institution of the reorganization proceedings, including claims for personal injury and property damage, (b) current liabilities and obligations of the Railroad Company and of any trustee or trustees of the estate incurred during the reorganization proceedings, and (c) all other claims, liabilities or obligations for which specific provision is not made in the Plan. To the extent that such claims, liabilities or obligations are not paid by the Railroad Company or any trustee or [137] trustees of the estate pursuant to order of the Court in the reorganization proceedings, they are to be paid in cash by the reorganized Company upon the consummation of the Plan, or assumed by the reorganized Company. All such claims, liabilities and obligations, including any claims arising from the disaffirmance of executory leases or other contracts by the Railroad Company or any trustee or trustees



of the estate in the reorganization proceedings pursuant to order of the court, in respect of which claims are filed or evidenced in accordance with orders of the Court, may be adjusted or compromised and dealt with or paid or discharged by the reorganized Company, all as may be determined by the Board of Directors of the reorganized Company and approved by the Court.

The reorganized Company shall be deemed to have assumed such of the contracts of the Railroad Company which are executory in whole or in part, including any executory leases and liabilities under guaranties, as shall have been affirmed by the Railroad Company or any trustee or trustees of the estate in the reorganization proceedings with the approval of the Court in the Reorganization Proceeding and prior to the date of confirmation of the Plan, and also any executory contracts made by the Railroad Company or any trustee or trustees of the estate with the approval of the Court in the reorganization proceedings which, by their terms, do not terminate at the conclusion of the reorganization proceedings.

## IX.

### Expenses of the Plan

All expenses of carrying out the Plan, and all costs of administration and other allowances made by the Court, shall be paid by the Railroad Company or by the reorganized Company subject to the provisions of Section 77 of the Bankruptcy Act and

shall constitute a charge upon the properties of the Railroad Company and the reorganized Company as a cost of administration prior in lien to all securities affected by the Plan. There shall be included in such expenses such reasonable compensation for necessary services rendered and reimbursement for actual expenses incurred [138] in connection with the proceeding and the Plan by the Trustees under the present First Mortgage, said Committee representing certain First Mortgage Bondholders (including reimbursement for actual expenses incurred in connection with said extension of the interest accruing during 1934 upon the existing First Mortgage Bonds) and by other parties in interest, committees or other representatives of creditors or stockholders, and the attorneys or agents of any thereof (including the Railroad Company), as may be approved by the Interstate Commerce Commission and the Court pursuant to the Bankruptcy Act; but the Plan shall not be construed as an offer or contract for such services independent of the Bankruptcy Act.

## X.

### Statements Contained in the Plan

All statements and figures herein contained with respect to the capitalization of the Railroad Company have been taken from its books or records, but no estimate, statement, explanation or suggestion contained in the Plan or in any circular issued, or which may hereafter be issued, by the Railroad

Company, or by any of its officers, is intended or is to be accepted as a warranty by the Railroad Company, or any of its directors or officers.

Dated as of January 1, 1936.

[Endorsed]: Filed Feb. 8, 1936. [139]

---

SUGGESTED  
PLAN OF REORGANIZATION  
OF  
THE WESTERN PACIFIC RAILROAD  
COMPANY

Effective Date, January 1, 1937.

The Committee which represents certain institutional holders of existing First Mortgage Bonds heretofore accepted the Plan proposed by the Railroad Company in the Reorganization Proceeding, conditioned on the acceptance of the Plan by the principal creditors of other classes. Such other classes of creditors having stated before the Interstate Commerce Commission that the Railroad Company's Plan was unacceptable to them without modifications which the Committee would regard as substantially adversely affecting the interests of the existing First Mortgage Bonds, and in the light of the past and probable future earnings of the Railroad Company's system, the Committee believes that the reorganization of the Railroad Company should follow substantially the lines of this Suggested Plan.

[140]



COMPARISON OF DISTRIBUTION OF ANNUAL INCOME UNDER SUGGESTED PLAN WITH THAT  
UNDER RAILROAD COMPANY'S PLAN OF JANUARY 1, 1936

Distributees	Suggested Plan (Effective as of January 1, 1937)			Railroad Company Plan (Effective as of January 1, 1936)	
	Assuming W. P. Corp. Furnishes New Money	Assuming RFC, RCC or ACJ Furnishes New Money	Assuming 1st Mtg. Bldgs. Furnish New Money	Income Bonds Not Converted	Income Bonds* Converted
Undisturbed	86,473	86,473	86,473	86,473	86,473
To First Mortgage Bondholders For New Money, pari passu	{394,320	{394,320	{394,320	{591,480	{591,480
To Others, pari passu	{None	{None	{None	{35,556	{35,556
Total Fixed Charges	880,793**	880,793**	880,793**	1,113,509**	1,113,509**
Capital Fund	500,000	500,000	500,000	500,000	500,000
To First Mortgage Bondholders for Contingent Interest	985,802	985,802	985,802	2,168,752	1,084,376
To Others pari passu	none	none	none	128,861	64,430
To Junior Debt for Contingent Interest	none	none	none	485,563	485,563
Total Interest Charges, plus Capital Fund	2,366,595	2,366,595	2,366,595	4,396,685	3,247,878
To First Mortgage Bondholders for Preferred Dividend	1,675,848	1,675,848	1,675,848	none	none
Sinking Fund for Income Bonds	197,160	197,160	197,160	104,437	104,437
Total before Common Stock	4,239,603	4,239,603	4,239,603	4,501,122	3,352,315
\$3 per share on Common Stock (before Preferred participates)	1,019,985	1,169,985	1,469,985***		
	5,259,588	5,409,588	5,709,588		
Excess over this total goes approximately					
To Existing First Mortgage Bondholders	45%	40%	75%	none	64%
To Others	55%	60%	25%	100%	36%

\*But earnings must exceed \$5,500,000 to warrant conversion.

\*\*Exclusive of interest upon any equipment obligations hereafter issued.

\*\*\*Of this amount approximately 61% would be paid on new Common Stock purchased by existing First Mortgage Bondholders to furnish new money.

[141]





**The Western Pacific Railroad Company****PLAN OF REORGANIZATION****Effective Date, January 1, 1934****I.****Introductory Statement**

The Western Pacific Railroad Company, a California corporation (hereinafter called the Railroad Company), prior to the Reorganization Proceeding hereinafter mentioned, owned and operated approximately 926 miles of main line track extending from San Francisco to Salt Lake City and approximately 106 miles of main line track extending from a connection at Keddie, California, with the line first mentioned, northerly to a connection with the lines of the Great Northern Railway Company near Bieber, California. This latter so-called Northern California Extension was constructed at a cost of slightly less than \$10,000,000 and put into operation on November 10, 1931. Its operation has materially added to the revenues of the System.

In addition to the foregoing main lines and various branch lines (together aggregating approximately 1,211 miles of road), the Railroad Company owned the entire capital stock and substantially all the outstanding indebtedness of the following subsidiaries:

- (1) Sacramento Northern Railway Company, an electrically operated, standard gauge, freight and passenger railroad, serving and con-

necting San Francisco and Oakland with Pittsburgh, Vacaville, Sacramento, Woodland, Marysville, Colusa, Oroville, Chico and other Sacramento Valley points. It also operates a street railway service in Sacramento, Marysville, Yuba City and Chico. Its lines aggregate approximately 276 miles of road. Its stock was acquired by the Railroad Company on November 9, 1925, and that portion of its line between Oakland and Sacramento was acquired as of January 1, 1929. Certain of its branches have been constructed since the latter date. Though its operations have resulted in a deficit before interest during each of the last five years, the Management of the Railroad Company advises that it contributes to the System a volume of traffic sufficient to justify its continued operation as part of the System.

(2) Tidewater Southern Railway Company owns, and operates a standard gauge, steam railroad connecting Stockton, California, with Manteca, Escalon, Modesto and Turlock in the San Joaquin Valley. Passenger service was abandoned in 1932. Its operations have resulted in income available for payment of interest on its indebtedness to the Railroad Company in every one of the last five years and have produced a surplus over all interest in each of those years, except 1931.

(3) Deep Creek Railroad Company owns and operates a standard gauge, steam railroad

from Wendover, Utah, to Cold Hill, Utah, a distance of 46 miles. While its operations during the last five years have shown a small deficit before interest, the Management of the Railroad Company advises that traffic furnished by it to the System justifies its continued operation.

(4). Standard Realty & Development Company handles land purchases and sales in connection with non-operating property, and its operations have resulted in a deficit in each of the last five years, in no case, however, exceeding \$10,000.

In addition, the Railroad Company owned jointly and equally with the Atchison, Topeka & Santa Fe Railroad and the Southern Pacific Railroad, the Central California Traction Company (acquired in 1928), an electrically operated railroad of about 53 miles between Stockton and Sacramento, California, with a branch line to Lodi, and jointly and equally with the Atchison, Topeka & Santa Fe, the Alameda Belt Line, (acquired in 1932), a standard gauge steam belt line of about 14 miles in the City of Alameda. As to each of [142] these companies the parent companies share equally operating deficits or profits, as well as advances for bond interest, sinking fund or additions and betterments. The Railroad Company, up to January 1, 1936, had been required to supply an aggregate of \$676,431 for those purposes since acquisition of its interests therein.

The Management of the Railroad Company reports that the consolidated net income of the System of the Railroad Company and its above-mentioned railroad subsidiaries, available for interest on funded debt, for the last ten years has been:

1926	\$4,759,282.22*
1927	2,647,493.79
1928	2,964,371.04
1929	2,529,946.36
1930	1,552,487.24
1931	186,707.68 Deficit
1932	252,706.16
1933	674,007.18
1934	1,084,243.85
1935	805,589.39

The Management points out, however, that in arriving at the foregoing figures an average of approximately \$140,000 per annum has been deducted for amortization of bond discount, and that during 1935 substantial extraordinary amounts were charged to maintenance in connection with laying of new rail, \$111,789 deducted from 1934 income under the Railroad Retirement Act was credited back to 1935 income.

The Management, in statements filed with the Interstate Commerce Commission, has estimated that the consolidated net income of the System of the Railroad Company and its subsidiaries, available for interest on funded debt (without however deducting that part of the estimated expense of the re-

---

\*The adequacy of maintenance expenditures in 1926 is questioned by the present management.



rehabilitation program hereinafter mentioned which, under the accounting rules of the Interstate Commerce Commission, would normally be chargeable to operating expense but which, it is expected, will be charged against surplus created as a result of the reorganization), will be:

Year	Available Income	Rehabilitation Operating Expense Not Deducted
1936	1,521,386**	1,747,284
1937	2,180,586	2,021,312
1938	2,738,886	1,280,074
1939	3,365,836	None
1940	3,769,836	None

The foregoing estimates of income available for interest on funded debt are also before deduction of any amount for the making of those routine additions and betterments (not included in the rehabilitation program) for which the issue of additional debt is of doubtful wisdom. The Management ad-

\*\*During the eight months ended August 31, 1936, the Consolidated Net Income of the System and its subsidiaries, available for interest on funded debt, similarly computed, was \$258,844.25. The amount of operating expense attributable to the rehabilitation program not deducted in arriving at this amount was \$1,169,880.09, so that the total amount available for interest under the accounting rules of the Interstate Commerce Commission for the first eight months of 1936 was a deficit of \$911,035.74. For the first eight months of 1935 the amount available for interest was a deficit of \$223,241.54, there being, however, no comparable operating expense attributable to the rehabilitation program during that period.

vises that provision should be made for such capital funds up to a maximum of \$500,000 per annum during the years 1936 to 1940, when the rehabilitation program will be in operation, and \$1,000,000 per annum during the years 1941 to 1945 inclusive. The necessity for such appropriation must be considered in determining the soundness of any capital structure proposed in the reorganization.

In 1927 the Railroad Company initiated an improvement or rehabilitation program contemplating the expenditure of \$18,000,000 over a five-year period. This program was partly carried out, with the following resultant expenditures:

	Maintenance		Investment Accounts	Total
	Way and Structures	Equipment		
1927	\$ 324,218	\$ 363,386	\$ 707,110	\$1,394,714
1928	931,336	374,345	988,123	2,293,804
1929	488,924	587,306	836,575	1,911,905
1930	537,421	174,040	808,331	1,519,793
1931	110,339	12,396	534,339	657,074
1932	Cr. 56,246	144	70,073	13,971
	\$2,335,092	\$1,511,617	\$3,944,551	\$7,791,261

Of the originally contemplated \$18,000,000 program, \$8,000,000 was estimated as Operating Expense.

Because of declining revenues, the rehabilitation program was substantially discontinued in 1931.

[143]

Having failed to pay any interest on its First Mortgage Bonds since September 1, 1933, the Railroad Company on August 2, 1935 filed in the United States District Court for the Northern District of California, Southern Division, its petition for reorganization under Section 77 of the Bankruptcy Act. The proceedings upon said petition are herein called the Reorganization Proceeding.

The Trustees appointed by the Court in the Reorganization Proceeding have obtained authority from the Court to proceed with the rehabilitation program, with a contemplated expenditure of approximately \$9,650,000, and have been authorized by the Court and the Interstate Commerce Commission to issue, and have issued, Trustees' Certificates having a lien prior to that of the existing First Mortgage, to provide the first \$3,000,000 toward this program. The rehabilitation program has been substantially approved by experts employed by Reconstruction Finance Corporation and by the Committee herein-after mentioned, for the purpose of making a physical examination of the property and a study of the program. These experts, however, have recommended that in addition to the expenditures contemplated by the Trustees, additional equipment should be purchased at an estimated cost of ap-

proximately \$3,750,000. A substantial part of this amount can be financed by equipment obligations and the remainder out of income contemplated to be applied to capital expenditures. Both the management and the representatives of the larger creditors and stockholders are, therefore, in agreement that there should be provided in any reorganization of the Railroad Company \$10,000,000 of new money with which to pay the outstanding Trustees' Certificates, to provide for the remainder of the rehabilitation program, and also to provide additional working capital.

Although the system of the Railroad Company has been valued by the Interstate Commerce Commission at approximately \$145,000,000, and although, as indicated above, the consolidated net income of the System available for fixed charges reached \$4,759,000\* in 1926, the more recent record of earnings, and the Management's forecast for the next five years, would seem to indicate the wisdom of keeping fixed interest charges after reorganization within \$1,000,000, and total interest charges, both fixed and contingent, within \$2,000,000.

As the foregoing amounts are insufficient to provide interest upon the \$49,290,100 of First Mortgage Bonds now outstanding, and the \$8,214,766 of unpaid interest which will have accrued thereon by January 1, 1937, and in addition interest on the required \$10,000,000 of new capital, it would seem

---

\*See footnote p. 2. [See page 54 of this printed record.]



that a sound capital structure can be insured only by allotting stock to the existing First Mortgage Bondholders for a portion of their present claims. Since all other classes of securities of the Railroad Company, other than the equipment obligations, are entirely junior in lien to the First Mortgage, obviously any stock so allotted to the present First Mortgage Bondholders (whether for principal or for accrued interest) should have rights as to both assets and income prior to those of the stock allotted such other creditors and stockholders of the Railroad Company.

This Plan has been prepared by Messrs. Frederick H. Ecker, John W. Stedman and Reeve Schley, as a Committee representing certain institutional holders of First Mortgage Bonds, as an application of the foregoing principles. It is believed that the Plan, if consummated, will result in a sound capital structure and that, in the distribution of the resultant securities, it fairly recognizes the relative rights and priorities of all the existing classes of the Railroad Company's security holders. The Plan contemplates that the opportunity to subscribe to new securities to supply the necessary \$10,000,000 of new money, offered, first, to The Western Pacific Railroad Corporation, as the Railroad Company's sole stockholder, second, to its junior creditors, and, third, to the present First Mortgage Bondholders, shall be upon terms sufficiently attractive to insure the raising of the new money.

The statements and figures herein contained with respect to the capitalization of the Railroad Com-

pany have been taken from the books and records furnished by the Management of the Railroad Company, but no estimate, statement, explanation or suggestion contained in the Plan or in any circular issued, or which may hereafter be issued, by the Committee, or by the Railroad Company, or by any of its officers, is intended or is to be accepted as a warranty. [144]

## II.

### Present Capital Liabilities as of January 1, 1937 (including unpaid interest)

		Fixed Annual** Interest
Equipment Trusts, Baldwin Lease and Pullman Contract	\$ 2,048,190	\$ 86,473
First Mortgage 5% Bonds due 1946:		
Principal	\$49,290,100	2,464,505
Unpaid Interest	8,214,766	
Total	57,504,866	
General and Refunding Mortgage 5% Bonds	18,999,500	
Pledged as follows:		
\$10,750,000 for Note to Reconstruction Finance Corporation,		
Principal	\$2,963,000	148,150
Unpaid Interest	427,564	
Total	\$3,390,564	
The Note to RFC is also secured by a second lien upon \$2,000,000 General and Refunding Mortgage Bonds pledged to secure the Note to RCC.		
\$4,000,000 for Note to The Railroad Credit Corporation,		
Principal	\$2,462,148	36,932**
Unpaid Interest	111,363	
Total	\$2,573,511	
The Note to RCC is also secured by a second lien upon the \$10,750,000 General & Refunding Bonds pledged to secure the Note to RFC and by a first lien upon the rights of the Railroad Company under the Marshalling and Distributing Plan of 1931.		
\$4,249,500 for Note to A. C. James Company,		
Principal	\$4,999,800	249,990
Unpaid Interest	749,970	
Total	\$5,749,770	

\$2,000,000 of the General and Refunding Bonds pledged to secure the Note to RCC were initially pledged to secure the Note to ACJ and by it re-

First Mortgage 5% Bonds due 1946:

Principal .....	\$49,290,100	2,464,505
Unpaid Interest .....	8,214,766	
Total .....	57,504,866	

General and Refunding Mortgage 5% Bonds .....

18,999,500

Pledged as follows:

\$10,750,000 for Note to Reconstruction Finance Corporation.

Principal .....	\$2,963,000	148,150
Unpaid Interest .....	427,564	
Total .....	\$2,390,564	

The Note to RFC is also secured by a second lien upon \$2,000,000 General and Refunding Mortgage Bonds pledged to secure the Note to RCC.

\$4,000,000 for Note to The Railroad Credit Corporation.

Principal .....	\$2,462,148	36,932**
Unpaid Interest .....	111,363	
Total .....	\$2,573,511	

The Note to RCC is also secured by a second lien upon the \$10,750,000 General & Refunding Bonds pledged to secure the Note to RFC and by a first lien upon the rights of the Railroad Company under the Marshalling and Distributing Plan of 1931.

\$4,249,500 for Note to A. C. James Company.

Principal .....	\$4,999,800	249,990
Unpaid Interest .....	749,970	
Total .....	\$5,749,770	

\$2,000,000 of the General and Refunding Bonds pledged to secure the Note to RCC were initially pledged to secure the Note to ACJ and by it repledged as additional collateral with the RCC.

Total Collateral Notes with Unpaid Interest \$11,713,845

Unsecured Obligations to The Western Pacific Railroad Corporation, including The Western Realty Company (with interest to January 1, 1937)	7,245,274	362,264
Preferred Stock .....	28,300,000	
Common Stock .....	47,500,000	
	\$161,597,830	\$3,348,314**

\*Does not include Equipment Trust which Trustees propose to issue in the near future in respect of additional equipment agreed upon as necessary.

\*\*Without interest on interest accrued and unpaid on First Mortgage Bonds or on RFC, RCC or ACJ Notes; and computing interest on said Notes rather than on their collateral, interest on the RCC Note being computed at 11½%, the New York Federal Reserve Bank rediscount rate as of April 20, 1936.



### III. Proposed New Capitalization

#### Summary

	Authorized	Presently Issued	Initial Charges
Undisturbed Equipment Trusts, Baldwin Lease and Pullman, Contract* .....	\$ 2,048,190	\$ 2,048,190	\$ 86,473
First Mortgage Bonds .....	50,000,000	19,858,020	794,320**
Total annual fixed charges .....			\$ 880,793
Income Mortgage 5% Bonds .....	19,716,040	19,716,040	985,802
Total annual interest charges, fixed and contingent .....			\$1,866,595
Participating 6% Preferred Stock .....	50,000,000	27,930,800	1,675,848
Total annual interest and dividend charges .....			\$3,542,443
Common Stock, without par value .....	500,000 shs.	Not less than 339,995 shs. nor more than 489,995 shs.	

\*See footnote page 4. [See page 62 of this printed record.]

\*\*Assuming that all such bonds bear interest at the rate of 4% per annum. As hereinafter provided the \$10,000,000 thereof to be issued to provide new money may bear interest at a rate not exceeding 5% per annum.

Institutional Bondholders et al.



### New First Mortgage Bonds

The new First Mortgage shall constitute a first lien upon the railroads and other property, real and personal, acquired by the New Company in the reorganization, including all interests of the Railroad Company, whether by way of stock, bonds or advances, in the other companies mentioned in the introductory statement.

Of the total authorized issue of \$50,000,000 new First Mortgage Bonds

\$9,858,020 are to be issued to the holders of existing First Mortgage Bonds in the reorganization;

\$10,000,000 are to be offered for subscription, with shares of new Common Stock as herein-after in Article V provided, to provide the new money required in the reorganization;

\$1,000,000 are to be authenticated forthwith and placed in the treasury of the New Company for issue for any proper corporate purpose;

\$29,141,980 are to be reserved to provide for, or to reimburse the New Company for, expenditures for additions, betterments, improvements or extensions made after January 1, 1937, in a principal amount not exceeding 75% of the actual cost of such additions, betterments, improvements or extensions.

The new First Mortgage Bonds may be issued in series which may differ as to date of maturity and interest rate. The Bonds to be issued under the Plan

shall be dated January 1, 1937, shall mature January 1, 1967, shall bear interest at the rate of 4% per annum, payable semi-annually, and shall be redeemable, in whole or in part, on any interest payment date upon 30 days' notice, at their principal amount and accrued interest except, however, that as hereinafter in Article V provided, the \$10,000,000 principal amount of new First Mortgage Bonds to be offered for subscription to provide the new money required in the reorganization may bear interest at a rate not exceeding 5% per annum, payable semi-annually, may mature not earlier than January 1, 1952, and may be redeemable at not exceeding 105% of their principal amount and accrued interest.

#### **New Income Mortgage 5% Bonds**

The new Income Mortgage shall constitute a lien, subject only to the lien of the First Mortgage, upon all property from time to time subject to the lien of the First Mortgage.

The entire authorized issue of \$19,716,040 new Income Mortgage 5% Bonds is to be issued to holders of existing First Mortgage Bonds in the reorganization.

The new Income Mortgage Bonds shall be dated January 1, 1937, shall mature January 1, 1987, and shall bear interest at the rate of 5% per annum, payable semi-annually, but, as hereinafter in this Article more fully provided, said interest shall be payable on October 1 and April 1 in each year, in respect of Income Periods ending the next pre-

ceding June 30 and December 31, respectively, and only out of Available Net Income of the New Company, and such interest shall be cumulative as against such Available Net In- [146] come for the Income Period in respect of which such interest is payable, and for the six Income Periods next succeeding such Income Period. Said Bonds shall be redeemable on any interest payment date at their principal amount, plus any interest payable thereon on such interest payment date.

As also hereinafter more fully provided there may be paid out of said Available Net Income, before payment of interest on the new Income Mortgage Bonds, certain amounts to provide a Contingency Reserve Fund and a Capital Fund.

As also hereinafter more fully provided the new Income Mortgage Bonds shall be entitled to the benefits of a 1% Cumulative Sinking Fund, payable out of Available Net Income remaining after any dividends paid therefrom on the new Participating 6% Preferred Stock.

#### New Participating 6% Preferred Stock

There will be authorized 500,000 shares of new Preferred Stock, each of the par value of \$100, of which 279,308 shares are to be issued to holders of the existing First Mortgage Bonds in the reorganization.

The new Preferred Stock shall be entitled to receive dividends at the rate of 6% per annum in respect of each calendar year, from January 1, 1937,

before any dividends shall be paid, or declared or set apart for payment, on the Common Stock. Such dividends shall be cumulative to the extent earned in respect of any calendar year but not paid; but such dividends shall otherwise be non-cumulative. After dividends shall have been paid or declared or set apart for payment, on the new Common Stock at the rate of \$3 per share in respect of any year, each share of new Preferred Stock shall be entitled to share equally with each share of new Common Stock in any dividends paid, or declared or set apart for payment, in respect of such year.

In any liquidation or winding up of the New Company, whether voluntary or involuntary, the new Preferred Stock shall be entitled to receive, out of the assets of the New Company, its par value, plus any accrued and unpaid cumulative dividends thereon, before any distribution shall be made to the new Common Stock but shall not be entitled to any further participation in such assets.

The new Preferred Stock shall be redeemable, in whole or in part, at any time at its par value plus accrued and unpaid cumulative dividends.

Holders of new Preferred Stock shall be entitled to voting power on all matters in respect of which stockholders of any class shall be entitled to vote, and shall further be entitled, voting separately as a class, to elect a majority of the Board of Directors of the New Company until full 6% dividends shall have been paid upon the new Preferred Stock for 5 successive calendar years, or until the number

of shares thereof outstanding shall have been reduced to less than 100,000 shares. Thereafter each share of new Preferred Stock shall be entitled to vote equally with each share of new Common Stock upon the election of Directors, and such election shall be by cumulative voting.

The New Company shall not, without the vote or consent of the holders of at least two-thirds in par value of the outstanding new Preferred Stock, (1) create or permit to be created any mortgage or other lien upon any of its properties, excepting the new First Mortgage, the new Income Mortgage or purchase money liens (including equipment obligations) upon property hereafter acquired, given for not more than 75% of the purchase price of such property; (2) create or issue any bonds, notes or other evidences of indebtedness maturing more than two years from their date, except purchase money obligations given for not more than 75% of the purchase price of property hereafter acquired; (3) create any stock ranking, either as to assets or dividends, in priority to, or on a parity with, the new Preferred Stock, or (4) permit any subsidiary, all of whose stock except directors' shares, shall be owned by the New Company, to create any mortgage or other lien upon any of its properties or issue any such bonds, notes or other evidences of indebtedness (except purchase money liens or obligations limited as aforesaid), or issue any additional stock of any class, unless the obligations secured by such mortgage or other lien or such other obligations or such stock shall be acquired by the New Company.



### **New Common Stock**

There will be authorized 500,000 shares of new Common Stock, without par value, of which 189,995 shares are to be issued forthwith and deposited in escrow for the benefit of Reconstruction Finance Corporation, The Railroad Credit Corporation and A. C. James Company, as hereinafter in Article IV provided. In addition, as hereinafter in Article V provided, a minimum of 150,000 shares and a maximum of 300,000 shares are to be issued forthwith and offered for subscription in connection with the \$10,000,000 of new First Mortgage Bonds to provide the new money required in the reorganization.

### **Application of Available Net Income**

Available Net Income shall be determined for each period of six months ending June 30 or December 31 (hereinafter called Income Periods) beginning with the Income Period ending June 30, 1937.

Available Net Income for each Income Period shall be determined by deducting from the consolidated income of the New Company and its subsidiaries available for fixed charges for such Income Period (determined in accordance with accounting rules of the Interstate Commerce Commission or other analogous Federal authority having jurisdiction in the premises at the time in force, or, to the extent not governed by such accounting rules, in accordance with sound accounting practice):

- (1) All fixed charges of the New Company and its subsidiaries accrued during such Income Period; and

(2) All other charges properly deductible from such income in determining income after fixed charges under such accounting rules then in force, but excluding contingent interest and Sinking Fund requirements, hereinafter provided for;

provided, however,

(a) that in determining Available Net Income there shall not be deducted any amounts expended in connection with the rehabilitation program out of the \$10,000,000 of new money to be provided in the reorganization (or out of the proceeds of any Trustees' Certificates or other obligations retired out of said new money), notwithstanding that under the accounting rules hereinbefore mentioned such expenditures may be chargeable as operating expenses\*; and

(b) if the New Company shall not come into ownership and possession of the properties now operated by the Trustees of the Railroad Company in the Reorganization Proceeding on or before January 1, 1937, Available Net Income

---

\*It is intended that the entire \$10,000,000 of new First Mortgage Bonds to be issued to provide new money, and the \$1,000,000 of new First Mortgage Bonds to be authenticated and placed in the treasury of the New Company, shall be issued against surplus created as a result of the reorganization, and approval by the Interstate Commerce Commission to charging the expenditures above referred to, commencing as of January 1, 1937, to surplus, rather than to operating expense, is to be requested.

for any period after January 1, 1937 until the New Company comes into possession and operation of such properties shall be computed as if the New Company had come into such ownership or possession on January 1, 1937 and had issued, as of that date, the new securities issuable under the Plan, other than the \$10,000,000, principal amount, of new First Mortgage Bonds to be issued to provide new money; and in lieu of interest on said Bonds there shall be charged the amount of interest actually accruing during such period upon any Trustees' Certificates or other obligations issued to provide funds for the rehabilitation program.

Available Net Income for each Income Period shall be applied to the following purposes and in the following order:

(1) If and to the extent that the Board of Directors of the New Company shall in its discretion so determine, to the maintenance at \$500,000 of the Contingency Reserve Fund (to be initially created out of new money as hereinafter provided), provided, however, that the amount applied to such purpose shall not exceed 10% of the Available Net Income for such Income Period.

(2) Any then remaining Available Net Income may, if the Board of Directors of the New Company in its discretion shall so determine, be applied to the creation of a Capital Fund to be

applied to, or to provide for, or to reimburse the treasury of the New Company for, Capital Investments (as defined by the Interstate Commerce Commission Classification of Income, Profit and Loss and General Balance Sheet Accounts for Steam Roads, Accounts Nos. 701, 702, 705 and 706 or such substituted accounts as may at the time be in effect, and including therein initial and principal payments upon equipment leased under equipment trusts or purchased under conditional sale agreements) to the extent that such Capital Investments have been made during the calendar year in which such Income Period is included, provided, however, that

(a) to the extent that expenditures are so provided for or reimbursed out of the Capital Fund, the New Company shall not thereafter have the right to issue any bonds or other evidences of indebtedness or any stock ranking, as to either assets or dividends, in priority to, or on a parity with, the new Preferred Stock, to capitalize or reimburse such expenditures;

(b) the amount set aside in the Capital Fund out of Available Net Income of any calendar year shall not exceed \$500,000 in respect of the calendar years 1937 to 1940, both inclusive; [148] \$1,000,000 in respect of the years 1941 to 1945, both inclusive; or, in respect of any subsequent year, more than 3% of the consolidated gross revenues of the

New Company and its subsidiaries for such calendar year; and

(c) Any unappropriated amount not charged out as of December 31 of the year in respect of which it shall have been set aside shall not be carried forward.

(3) Any then remaining Available Net Income shall be applied to the payment on October 1 and April 1 each year, commencing October 1, 1937, of interest on the then outstanding new Income Mortgage 5% Bonds (not including any thereof theretofore purchased or redeemed out of the Sinking Fund hereinafter in clause (5) provided for) accruing during the Income Period ending on the next preceding June 30 or December 31, respectively, and, to the extent unpaid, any interest which shall have accrued on said Bonds in respect of six Income Periods next preceding such Income Period.

(4) Any then remaining Available Net Income shall be applied, if, and to the extent that, such dividends shall be declared by the Board of Directors of the New Company, to the payment on April 1 of each year, commencing April 1, 1938, of dividends at the rate of 6% per annum upon the new Preferred Stock in respect of the two Income Periods ending on the next preceding December 31, to the extent not theretofore paid, and of any accrued and unpaid cumulative dividends on the new Preferred Stock; and, if and to the extent so declared, to the



payment on October 1 in each year, commencing October 1, 1937, of interim dividends on the new Preferred Stock at the rate of 6% per annum in respect of the Income Period ending on the next preceding June 30, and of any such accrued and unpaid cumulative dividends.

(5) Any then remaining Available Net Income shall then be applied to the creation on October 1 and April 1 in each year, commencing October 1, 1937, of a Cumulative Sinking Fund, in an amount up to, but not exceeding, in respect of any calendar year, 1% of the total principal amount of new Income Mortgage Bonds issued in the reorganization plus an amount equal to interest on any Income Mortgage Bonds theretofore purchased or redeemed out of the Sinking Fund calculated at the rate paid (pursuant to the foregoing clause (3)) in respect of such calendar year, including accumulations, upon outstanding Income Mortgage Bonds. Said Sinking Fund shall be applied to the purchase of new Income Mortgage Bonds at not exceeding their redemption price, and whenever the amount in the Sinking Fund exceeds \$50,000 and new Income Mortgage Bonds are not tendered or cannot otherwise be purchased at less than their redemption price, the funds then in the Sinking Fund shall be applied to the redemption of the new Income Mortgage Bonds on the next succeeding interest payment date. Bonds purchased or re-

deemed out of the Sinking Fund shall not thereafter be re-issued.

(6) Any then remaining Available Net Income may be applied to any proper corporate purpose of the New Company, including (but only after all accrued and unpaid cumulative dividends on the new Preferred Stock to the next preceding June 30 or December 31, as the case may be, shall have been paid, or declared and set apart for payment) dividends on the New Common Stock and participating dividends on the new Preferred Stock, in accordance with their respective rights as hereinbefore provided.

#### IV.

##### Treatment of Existing Securities

1. Existing Equipment Trusts, Baldwin Lease and Pullman Contract, aggregating \$2,048,190, shall remain undisturbed and shall be assumed by the New Company.

2. Holders of existing First Mortgage 5% Bonds (with March 1, 1934, and subsequent coupons) shall receive for each \$1,000, principal amount, of such Bonds:

(a) \$200 of new First Mortgage 4% Bonds;

(b) \$400 of new Income Mortgage 5% Bonds;

(c) \$400 of new Participating 6% Preferred Stock;

(d) \$166.66 $\frac{2}{3}$  of new Participating 6% Preferred Stock (being of par value equal to the

amount of interest on the existing Bonds accrued to January 1, 1937); and

(e) subject to the terms and conditions hereinafter in Article V provided, the contingent right to subscribe for new First Mortgage Bonds and new Common Stock to be issued to provide new money. [149].

3. Notes to Reconstruction Finance Corporation, The Railroad Credit Corporation and A. C. James Company, together with interest accrued thereon to January 1, 1937, shall be dealt with as follows:

189,995 shares of new Common Stock shall be deposited with a Depositary under an Escrow Agreement for the benefit of Reconstruction Finance Corporation, The Railroad Credit Corporation and A. C. James Company, as hereinafter provided, and there shall be issued to said corporations, respectively, registered Escrow Certificates evidencing their respective rights under the Escrow Agreement. Said Certificates shall be in such form as may be determined by the Committee (hereinafter in Article VIII, provided for), and shall be transferable upon presentation thereof for transfer at the office of the Escrow Depositary accompanied by appropriate instruments of assignment and transfer duly executed by the registered holder of such surrendered Certificate or Certificates. As hereinafter used, "RFC", "RCC", and "ACJ"

mean the registered holder of the Escrow Certificates issued to Reconstruction Finance Corporation, The Railroad Credit Corporation and A. C. James Company, respectively. If the New Company shall purchase or acquire any of said Escrow Certificates, it may become the registered holder thereof and succeed to all the rights of a registered holder of such Escrow Certificates, and shall thereupon be embraced in said terms as herein used.

RFC shall be entitled to receive, upon surrender of its Escrow Certificate at the office of the Escrow Depositary, on January 1, 1942, either

(1) an amount in cash equal to \$3,390,564, plus interest thereon at the rate of 4% per annum from January 1, 1937, less the amount of any cash paid to it as hereinafter in this Article IV provided, or

(2) if such amount be not paid to it on January 1, 1942, as hereinafter provided, 107,500 shares of new Common Stock.

If the amount to be paid to RFC on January 1, 1942, as aforesaid, is not deposited with the Escrow Depositary by the New Company on or before December 1, 1941, it may be so deposited by RCC, and if it is not so deposited by RCC on or before December 15, 1941, it may be so deposited by ACJ on or before January 1, 1942. If such deposit is made by the New Company,

or by RCC, or by ACJ, the amount thereof shall be paid by the Escrow Depositary to RFC on January 1, 1942, and said 107,500 shares of new Common Stock shall continue to be held by the Escrow Depositary for delivery as hereinafter provided. If such deposit is not made on or before January 1, 1942, the Escrow Depositary shall deliver to RFC said 107,500 shares of new Common Stock.

RCC shall be entitled to receive, upon surrender of its Escrow Certificate at the office of the Escrow Depositary on January 1, 1943, either

(1) an amount in cash equal to \$2,573,511, plus interest thereon at the rate of 4% per annum from January 1, 1937, less the amount of any cash paid to it, as hereinafter provided, less also any amount paid to RCC on account of the Railroad Company's rights under the Marshalling and Distributing Plan, 1931 (plus any amount deposited by RCC for payment on January 1, 1942, to RFC as aforesaid, with interest thereon at the rate of 4% per annum from the date of such deposit), or

(2) if such amount be not paid to it on January 1, 1943, as hereinafter provided, 40,000 shares of new Common Stock, and if said 107,500 shares of new Common Stock have not been delivered to RFC as hereinbefore provided, said 107,500 shares of new Common Stock.



If the amount to be paid to RCC on January 1, 1943, as aforesaid, is not deposited with the Escrow Depositary by the New Company on or before December 15, 1942, it may be so deposited by ACJ on or before January 1, 1943. If such deposit is made by the New Company or by ACJ, the amount thereof shall be paid by the Escrow Depositary to RCC on January 1, 1943, and said 40,000 shares of new Common Stock (and also said 107,500 shares of new Common Stock if not already delivered to RFC) shall continue to be held by the Escrow Depositary for delivery as hereinafter provided. If such deposit is not made on or before January 1, 1943, the Escrow Depositary shall deliver to RCC said 40,000 shares of new Common Stock, and, if said 107,500 shares of New Common Stock have not been delivered to RFC as hereinbefore provided, also said 107,500 shares of new Common Stock.

ACJ shall be entitled to receive, upon surrender of its Escrow Certificate at the office of the Escrow Depositary on January 1, 1944, either [150]

(1) an amount in cash equal to \$5,749,770, plus interest thereon at the rate of 4% per annum from January 1, 1937, less the amount of any cash paid to it, as hereinafter provided (plus any amount deposited by ACJ for payment on January 1, 1942, to RFC as aforesaid, plus any amount deposited by ACJ

for payment on January 1, 1943, to RCC as aforesaid, in each case with interest thereon at the rate of 4% per annum from the date of such deposit), or

(2) if such amount be not paid to it on January 1, 1944, as hereinafter provided, 42,495 shares of new Common Stock, and, if said 107,500 shares of new Common Stock have not been delivered to RFC or RCC, as hereinbefore provided, said 107,500 shares of new Common Stock; and if said 40,000 shares of new Common Stock have not been delivered to RCC, as hereinbefore provided, said 40,000 shares of new Common Stock.

The amount to be paid to ACJ on January 1, 1944, as aforesaid, may be deposited with the Escrow Depositary by the New Company on or before January 1, 1944, and, if so deposited by the New Company, the amount thereof shall be paid by the Escrow Depositary to ACJ on January 1, 1944, and all of the shares of new Common Stock then on deposit with the Escrow Depositary shall be delivered by the Escrow Depositary to or on the order of the New Company. If such deposit is not made on or before January 1, 1944, the Escrow Depositary shall deliver to ACJ said 42,495 shares of new Common Stock, and, if said 107,500 shares of new Common Stock shall not have been delivered to RFC or RCC as hereinbefore provided, also said 107,500 shares of new Common Stock, and,

if said 40,000 shares of new Common Stock shall not have been delivered to RCC as hereinbefore provided, also said 40,000 shares of new Common Stock.

Until payment of cash or delivery of shares of new Common Stock to RFC, RCC and ACJ, the Escrow Depositary shall, from time to time, pay any cash dividends received upon the shares of new Common Stock deposited with it to RFC, RCC and ACJ in the same proportions in which the proceeds of the sale of such shares are required to be distributed, as hereinafter provided.

The New Company may at any time at its option, upon 30 days' notice to the registered holders of Escrow Certificates at the time outstanding, redeem such outstanding Escrow Certificates by depositing with the Escrow Depositary for the account of the registered holders of such outstanding Escrow Certificates an amount in cash equal to the total cash amount at the time represented by such outstanding Escrow Certificates, (including interest at the rate of 4% per annum, and any amount which, at that time may have been deposited by RCC or ACJ, as hereinbefore provided, for payment to RFC or RCC, with interest thereon at the rate of 4% per annum to the date of such deposit, and deducting any cash previously paid thereon as herein provided), and upon such redemption and deposit the Escrow Depositary

shall pay said amounts in cash to the respective holders of outstanding Escrow Certificates and shall deliver all the new Common Stock then on deposit, to or on the order of the New Company.

Purchase Warrants shall be issued (to or on the order of The Western Pacific Railroad Corporation, as hereinafter provided) entitling the holders thereof to purchase on or before December 1, 1941, all or any part of said 189,995 shares of new Common Stock at the price of \$62 per share, plus interest thereon at the rate of 4% per annum from January 1, 1937, to a date 10 days after the exercise of such Purchase Warrants. Unless the New Company shall theretofore have deposited with the Escrow Depositary the amount necessary to redeem all the outstanding Escrow Certificates, as hereinbefore provided, the proceeds of the exercise of such Purchase Warrants shall be paid to the Escrow Depositary and the Escrow Depositary shall deliver, out of the new Common Stock deposited with it, as hereinbefore provided, new Common Stock so paid for upon the exercise of such Purchase Warrants and shall, within 10 days thereafter, pay to RFC, RCC and ACJ such cash in the proportions of 56.581% to RFC, 21.053% to RCC and 22.366% to ACJ, until the cash amount payable in respect of RFC Escrow Certificate shall have been paid in full, and there-

after in the proportions of 77.634% to RCC and 22.366% to ACJ, until the cash amount payable in respect of RCC Escrow Certificate shall have been paid in full, and thereafter all such proceeds shall be paid to ACJ until the cash amount payable in respect of ACJ Escrow Certificate shall have been paid in full. Any excess of cash paid upon the exercise of Purchase Warrants shall be paid to the New Company.

The amounts of any new Common Stock deliverable upon the exercise of Purchase Warrants shall be taken from the stock deliverable to RFC, RCC and ACJ, as hereinbefore provided, in the same proportions; and the amount of stock which may thereafter become deliverable to them, as hereinbefore provided, shall be correspondingly reduced. [151]

If the New Company shall have exercised the right to redeem the Escrow Certificates as hereinbefore provided, the proceeds of the exercise of the Purchase Warrants shall be paid to it, and, upon such payment, it shall issue and deliver the new Common Stock issuable in respect of such Purchase Warrants.

Subject to the terms and conditions hereinafter in Article V provided, Reconstruction Finance Corporation, The Railroad Credit Corporation and A. C. James Company shall also have the contingent right to subscribe for new First Mortgage Bonds and new Common Stock to be issued to provide new money.



4. The Western Pacific Railroad Corporation, as the holder of substantially the entire unsecured debt and all the outstanding Preferred and Common Stock of the Railroad Company, shall receive, upon release and surrender of said indebtedness and stock:

(a) Purchase Warrants issued under the Escrow Agreement, as hereinbefore provided, in respect of 189,995 shares of new Common Stock; and

(b) Subscription Warrants for \$10,000,000 of new First Mortgage Bonds and 150,000 shares of new Common Stock, to be issued to provide new money, as hereinafter in Article V provided, at the price of \$100 and accrued interest on said Bonds, for each unit of \$100 of new First Mortgage Bonds and  $1\frac{1}{2}$  shares of new Common Stock.

## V

### Provision for New Money

\$10,000,000 of new money is required by the New Company for the following purposes:

\$3,000,000 to retire Trustees' Certificates issued to provide for the 1936 expenditures under the rehabilitation program;

\$6,500,000 for completion of the rehabilitation program (or to retire any further Trustees' Certificates or other obligations issued to provide therefor), or to the extent that the Board of Directors may so determine, for other addi-

tions and betterments, or to provide for fixed charges for which the New Company cannot, in the opinion of the Board of Directors, provide without unduly impairing working capital;

\$500,000 as a Contingency Reserve Fund, to be available only for the purpose of paying fixed interest charges, principal of and dividends on equipment trust obligations, and operating expenses which cannot otherwise be provided for, without, in the opinion of the Board of Directors, unduly impairing working capital.

To provide said \$10,000,000 there will be issued to or on the order of The Western Pacific Railroad Corporation Subscription Warrants, in such form as may be determined by the Committee, evidencing the right to subscribe for an aggregate of

\$10,000,000 of new First Mortgage Bonds and

150,000 shares of new Common Stock.

at the price of \$100, plus accrued interest on said Bonds, for each unit of

\$100 of new First Mortgage Bonds and

1½ shares of new Common Stock.

It is contemplated that the bonds to be covered by the Subscription Warrants shall be dated January 1, 1937, shall mature January 1, 1967, shall bear interest at the rate of 4% per annum, payable semi-annually, and shall be redeemable in whole or in part on any interest payment date upon thirty days' no-

tice at their principal amount and accrued interest; but if the Committee shall determine that it is advisable, in order to insure the raising of the new money, and to that end to obtain underwriting of the offerings provided for in this Article V, the Committee may, with the approval of the Interstate Commerce Commission and of the Court in the Reorganization Proceeding, cause the First Mortgage Bonds so to be offered to bear interest at a greater rate, but not exceeding 5% per annum, payable semi-annually, to mature at an earlier date, but not earlier than January 1, 1952, and to be redeemable at a higher price, but not exceeding 105% of their principal amount and accrued interest. [152]

Such subscription Warrants shall entitle the holders thereof to subscribe for said units at said price for a period to be specified therein, and which, as to not less than \$7,000,000 principal amount of Bonds represented thereby, shall be not less than 60 nor more than 120 days after the date of final confirmation of the Plan by the Court in the Reorganization Proceeding, and as to any remainder of said \$10,000,000 of Bonds may, if the Board of Directors of the New Company shall so determine, be a further period expiring not later than December 31, 1937.

Opportunity to provide such part of the new money as is not provided by the exercise of said Subscription ~~Warrants~~ shall be offered to Reconstruction Finance Corporation, The Railroad Credit Corporation and A. C. James Company in propor-

tion to the General and Refunding Mortgage Bonds now held by them, that is to say, in the proportions of 56.581% to Reconstruction Finance Corporation, 21.053% to The Railroad Credit Corporation, and 22.366% to A. C. James Company. Said corporations shall be entitled to provide their respective portions of such new money, by subscribing for such new First Mortgage Bonds as are covered by the Subscription Warrants expired and not exercised, together with new Common Stock, at the price of \$100, plus accrued interest on said Bonds, for each unit of \$100 of new First Mortgage Bonds and

2 shares of new Common Stock:

If any of said corporations shall fail to subscribe for its full proportion as aforesaid, the other or others of said corporations may subscribe for the unsubscribed balance, in the proportion which the existing General and Refunding Mortgage Bonds of the Railroad Company held by them respectively bear to the total amount of General and Refunding Mortgage Bonds held by the corporations so electing to subscribe for their full proportion.

The contingent rights of subscription thus granted to Reconstruction Finance Corporation, the Railroad Credit Corporation and A. C. James Company shall be evidenced by appropriate Warrants in such form as may be determined by the Committee, and such rights shall, in the case of each offering, run concurrently with the rights evidenced by the Subscription Warrants to be issued to, or on the order

of, The Western Pacific Railroad Corporation. Holders of such Warrants will be required to elect prior to the expiration of such Subscription Warrants, in each case, the extent to which they will exercise their subscription rights. Notice of the amount of new First Mortgage Bonds and new Common Stock allotted against such subscriptions will be given by registered mail as promptly as possible after the expiration of the Subscription Warrants in each case, and payment for such allotments will be required to be made at a bank or trust company in New York City, to be specified in such notice, within ten days after the mailing of such notice. Upon failure of any holder of such Warrant to take up and pay for the new First Mortgage Bonds and new Common Stock allotted to it, at the price hereinbefore provided, the holder of such Warrant shall cease to have any rights in respect of such new First Mortgage Bonds and new Common Stock.

Should holders of the Subscription Warrants fail to exercise any thereof and Reconstruction Finance Corporation, The Railroad Credit Corporation and A. C. James Company provide the entire \$10,000,000 of required new money, there would thus be issued, to provide said new money, an aggregate of \$10,000,000 of new First Mortgage Bonds and 200,000 shares of new Common Stock.

If holders of the Subscription Warrants, Reconstruction Finance Corporation, The Railroad Credit Corporation and A. C. James Company fail to pro-



vide all or any part of said \$10,000,000 of new money, as aforesaid, holders of the existing First Mortgage Bonds of the Railroad Company shall be entitled to provide the same by subscribing for new First Mortgage Bonds and new Common Stock at the price of \$100, plus accrued interest on said Bonds, for each unit of

\$100 of new First Mortgage Bonds and  
3 shares of new Common Stock.

The contingent rights of subscription thus granted to holders of existing First Mortgage Bonds shall be evidenced by appropriate Warrants in such form as may be determined by the Committee and such rights shall, in the case of each offering, run concurrently with the rights evidenced by the Subscription Warrants to be issued to, or on the order of, The Western Pacific Railroad Corporation. Holders of such Warrants shall be [153] entitled, upon each offering, to subscribe for as many of said units as they may elect, but if there shall be an oversubscription by the holders of such Warrants, the Committee shall allot the new First Mortgage Bonds and new Common Stock in the proportion which the respective holdings of First Mortgage Bonds of the Railroad Company held by the respective original issues of the exercised Warrants bear to the total amount of such Bonds held by the original issues of all the Warrants so exercised. Notice of the amount of new First Mortgage Bonds and new Common Stock allotted against such subscriptions

will be given, in respect of each offering, by registered mail as promptly as possible after the expiration of the rights of Reconstruction Finance Corporation, The Railroad Credit Corporation and A. C. James Company to take up and pay for their allotments as hereinbefore provided; and payments for the allotments against such subscriptions will be required to be made at a bank or trust company in New York City, to be specified in such notice within ten days after the mailing of such notice. Upon failure of any holder of such Warrant to take up and pay for the new First Mortgage Bonds and new Common Stock allotted to it, at the price hereinbefore provided, the holder of such Warrant shall cease to have any rights in respect of such new First Mortgage Bonds and new Common Stock.

Should holders of the Subscription Warrants, Reconstruction Finance Corporation, The Railroad Credit Corporation, and A. C. James Company provide none of the \$10,000,000 of required new money, there would thus be issued, to provide said new money, an aggregate of

\$10,000,000 of new First Mortgage Bonds and  
300,000 shares of new Common Stock.

New First Mortgage Bonds issued to provide new money will be issued and allotted in multiples of \$100 and no subscription for fractional amounts of \$100 will be received.

The Committee or the New Company may in their discretion effect such arrangements for underwrit-

ing the exercise of all or any part of the foregoing subscription rights upon such terms and conditions as they may determine, with the approval of the Interstate Commerce Commission and of the Court in the Reorganization Proceeding. If such arrangements for underwriting shall be made with Reconstruction Finance Corporation, the compensation for such underwriting may be, or include, the exchange by the New Company of new Income Mortgage Bonds and new Participating Preferred Stock, in such proportions as the Committee with like approval shall determine, in exchange for the RFC Escrow Certificate, to be issued to Reconstruction Finance Corporation as provided in Article IV hereof. Such exchange, however, shall not constitute a cancelation of said RFC Escrow Certificate, or be deemed equivalent to a deposit by the New Company of cash against said RFC Escrow Certificate, as contemplated by said Article IV; but the New Company shall succeed to all the rights of Reconstruction Finance Corporation in respect of the RFC Escrow Certificate under said Article IV. [154]

## VI

## Table of Distribution of New Securities

Present Liabilities as of July 1, 1936	Amount	Undisturbed	New First Mortgage Bonds	New Income Mortgage 5% Bonds	New Participating 6% Preferred Stock	New Common Stock
Equipment Trusts, Baldwin Lease and Pullman Contracts	\$ 2,048,190	\$2,048,190				
First Mortgage 5% Bonds due 1946	49,290,100		\$ 9,858,020 (20%)	\$19,716,040 (40%)	\$19,716,040 (40%)	
First Mortgage Bond Interest (Unpaid)	8,214,766				8,214,766	
New Money			\$10,000,000			Not less than 150,000 nor more than 300,000 shares, (See Article V)
General & Refunding Bonds						
RFC for \$2,963,000 Note 426,753 Int. }	750,000					Escrow Ctfs. for 107,500 shares (See Article IV)
\$3,882,753						
RCC for \$2,482,218 Note 114,156 Int. }	4,000,000					Escrow Ctfs. for 40,000 shares (See Article IV)
\$2,596,374						
ACJ for \$4,999,800 Note 749,870 Int. }	4,249,500					Escrow Ctfs. for 42,495 shares (See Article IV)
\$5,749,670						
The Western Pacific R. R. Corporation, for						
Advances (including Realty Co.)	7,245,274		Subscription Warrants for above mentioned			Purchase Warrants for above mentioned 189,995 shares (See Article IV)
Preferred Stock	28,300,000		\$10,000,000 (See Article V)			Subscription Warrants for above mentioned 150,000 shares (See Article V)
Common Stock	47,500,000					
Aggregate principal	\$161,597,830	\$2,048,190	\$19,858,020	\$19,716,040	\$27,930,806	Not less than 339,995 shares Not more than 489,995 shares
Annual fixed charges	\$ 3,348,314*	\$ 86,473	\$794,320**			
Annual contingent interest				\$ 985,802		
Annual Preferred 6% dividend					\$ 1,675,848	

\* Without interest on interest accrued and unpaid on First Mortgage Bonds, or on RFC, RCC or ACJ Notes; and computing interest on said Notes rather than on their collateral interest on the RCC Note being computed at  $1\frac{1}{2}\%$  per annum, the N. Y. Federal Reserve Bank rediscount as of April 20, 1936.

\*\* Assuming that all such Bonds bear interest at the rate of 4% per annum. As hereinbefore in Articles III and V provided the \$10,000,000 thereof to be issued to provide new money may bear interest at a rate not exceeding 5% per annum.





## VII.

## Claims Not Affected by the Plan

The following claims are not affected by the Plan: (a) current liabilities of the Railroad Company incurred in the ordinary conduct of its business prior to the institution of the Reorganization Proceeding, including claims for personal injury and property damage, (b) current liabilities and obligations of the Railroad Company and of any trustee or trustees of the estate incurred during the Reorganization Proceeding, and (c) all other claims, liabilities or obligations for which specific provision is not made in the Plan. To the extent that such claims, liabilities or obligations are not paid by the Railroad Company or any trustee or trustees of the estate pursuant to order of the Court in the Reorganization Proceeding, they are to be paid in cash or assumed by the New Company. All such claims, liabilities, and obligations, including any claims arising from the disaffirmance of executory leases or other contracts of the Railroad Company or any trustee or trustees of the estate in the Reorganization Proceeding pursuant to order of the Court, in respect of which claims are filed or evidenced in accordance with orders of the Court, may be adjusted or compromised and dealt with or paid or discharged by the New Company, all as may be justed or compromised and dealt with or paid or discharged by the New Company, all as may be determined by the Board of Directors of the New Company and approved by the Court.

The New Company shall be deemed to have assumed such of the contracts of the Railroad Company which are executory in whole or in part, including any executory leases and liabilities under guaranties, as shall have been affirmed by the Railroad Company or any trustee or trustees of the estate in the Reorganization Proceeding with the approval of the Court in the Reorganization Proceeding and prior to the date of confirmation of the Plan, and also any executory contracts made by the Railroad Company or any trustee or trustees of the estate with the approval of the Court in the Reorganization Proceeding which, by their terms, do not terminate at the conclusion of the Reorganization Proceeding.

### VIII.

#### Method of Participation in, and Consummation of, the Plan

No holder of any security of the Railroad Company affected by the Plan shall be requested to accept the Plan until after a public hearing upon the Plan, held as provided by Section 77 of the Bankruptcy Act as it now exists or may hereafter be amended (hereinafter called Section 77), and a report and order of the Interstate Commerce Commission approving the Plan (in its present form or as it may be modified as hereinafter provided) and finding that the Plan complies with said Section 77, or until the Court in the Reorganization Proceeding shall have taken such action as may be

required by Section 77 prior to the submission of a plan thereunder to the security holders of the Railroad Company. Thereafter the Plan shall be submitted to the security holders of the Railroad Company in accordance with the provisions of said Section 77.

The Plan shall not be carried out until it shall have been accepted by or on behalf of the holders of at least two-thirds in principal amount of the outstanding existing First Mortgage 5% Bonds of the Railroad Company, nor unless either (1) the Plan shall have been accepted by or on behalf of the creditors of each class, as the same may be classified by the Court in the Reorganization Proceeding, holding at least two-thirds in principal amount of the total allowed claims of such class, and by or on behalf of the stockholders of each class holding at least two-thirds of the stock of such class, or (2) provision shall have been made for protecting the interests of such non-assenting classes of creditors and stockholders, as hereinafter in Article IX provided.

Messrs. Frederick H. Ecker, John W. Stedman and Reeve Schley have heretofore acted as a Committee to represent certain large institutional holders of existing First Mortgage Bonds, being not more than 25 bona fide holders thereof, in respect of the extension of interest maturing during 1934 upon such First Mortgage Bonds, in respect of the performance of the Railroad Company's agreements made in connection with said extension, in

the negotiation of the plan of reorganization heretofore submitted by the Railroad Company in the Reorganization Proceeding, and in the preparation of this Plan. If, and when, this Plan shall be submitted to [156] the security holders of the Railroad Company for their acceptance or rejection, as hereinbefore provided, said Committee shall comply with the provisions of said Section 77 to qualify it to act as the representative of all holders of existing First Mortgage 5% Bonds of the Railroad Company assenting to the Plan, and otherwise to perform the duties and exercise the rights provided in the Plan.

The Plan may be carried out either by re-vesting the properties formerly of the Railroad Company in the Railroad Company or by transferring said properties to a new corporation organized for the purpose, and the execution by the corporation in which such properties are vested of the new mortgages and the issue by it of the new securities contemplated by the Plan. The corporation so acquiring said properties and issuing the new securities is herein referred to as the New Company.

The method of carrying out the Plan shall be determined by the Committee in its discretion, and the Committee shall also determine the form, and, except as herein otherwise expressly provided, the provisions, of all mortgages, bonds, coupons, charters, by-laws, stock certificates, purchase warrants, subscription warrants, acceptances, assents, and all other instruments in the judgment of the Committee

necessary or desirable in connection with carrying out the Plan.

The Committee may from time to time add to its members, and any vacancy from time to time occurring in the Committee may be filled by the remaining members of the Committee. The Committee may act by a majority of its members as from time to time constituted, at a meeting or in writing without a meeting. The Committee may employ such agents, attorneys and others as it may deem desirable for the purposes of the Plan. The Committee may from time to time delegate to others any power or discretion conferred upon it by the Plan; and the members of the Committee shall not be liable for any action taken by them in good faith or by any person employed by the Committee in good faith, or otherwise, except for their respective individual malfeasance or neglect.

The Committee may from time to time, whether before or after acceptance of the Plan by the holders of securities, modify the Plan or adopt a substitute plan, in accordance with, and subject to, the provisions of said Section 77; and the term "Plan" as used herein shall be deemed to include any such modification or substitute plan.

The members of the Committee have agreed to serve without compensation, but the expenses of the Committee shall be reimbursed as hereinafter provided.

Unless otherwise provided in said Section 77 or any order or orders of the Court in the Reorgani-



zation Proceeding or of the Interstate Commerce Commission, whenever notice shall be required or permitted to be given under or pursuant to the Plan, such notice shall be given by publishing a copy of such notice once in each week in one newspaper published and of general circulation in the Borough of Manhattan, the City and State of New York, and in one newspaper published and of general circulation in the City of San Francisco, State of California, and also (1) in case of notices to security holders who have accepted the Plan, by mailing such notice, postage prepaid, to the addresses of such security holders set forth in the acceptances signed by them; and (2) in case of notices to security holders who shall not have accepted the Plan, by mailing such notice, postage prepaid, to such security holders whose names and addresses appear on the books of the Railroad Company or of the New Company, as the case may be.

## IX.

### Provision for Dissenting Creditors and Stockholders

If the holders of more than one-third in principal amount of any class of creditors of the Railroad Company, as they may be classified by the Court in the Reorganization Proceeding, or the holders of more than one-third of the shares of stock of any class of the Railroad Company shall not have accepted the Plan within such period as the Com-

mittee, with the approval of the Commission and the Court, may determine after holders of at least two-thirds in principal amount of the existing First Mortgage 5% Bonds of the Railroad Company shall have accepted the Plan, the property of the Railroad Company shall be sold at public auction at a fair upset price as determined by the Court in the Reorganization Proceeding, and the non-[157] assenting creditors of such class or the non-assenting stockholders of such class, as the case may be, shall be entitled to receive their aliquot portion of the proceeds of the sale of such property, after deducting therefrom all expenses of such sale and the amount which would be required to pay in full, principal and interest to the date of such sale, all creditors whose claims are prior in lien or superior in equity to the claims of such non-assenting creditors or the rights of such non-assenting stockholders.

Upon any such sale, the property shall be purchased for the benefit of the New Company, in the reorganization by the Committee, or by a purchaser nominated by the Committee, and there shall be applied on account of the purchase price the distributive share of the proceeds of sale of all securities the holders of which have assented to the Plan, and the securities, though not assenting to the Plan, of all classes two-thirds or more in amount of which have assented to the Plan.

## X.

## Expenses of the Reorganization

All expenses in connection with the Plan and its consummation, and all costs of administration and other allowances made by the Court in the Reorganization Proceeding, shall be paid by the New Company, subject to the provisions of Section 77 of the Bankruptcy Act, and shall constitute a charge upon the properties of the New Company as a cost of administration prior in lien to all new securities issued under the Plan.

There shall be included in such expenses such reasonable compensation for necessary services rendered and reimbursement for actual expenses incurred in connection with the Reorganization Proceeding and the Plan by the Trustees under the present First Mortgage and the present General and Refunding Mortgage of the Railroad Company, the Committee (including reimbursement for actual expenses incurred by the Committee in connection with the extension of interest on the existing First Mortgage 5% Bonds accruing during 1934, in respect of the performance of the Railroad Company's agreements made in connection with said extension, in the negotiation of the plan heretofore proposed by the Railroad Company in the Reorganization Proceeding, and in connection with this Plan); and by other parties in interest, committees or other representatives of creditors and security holders of the Railroad Company, and the

attorneys or agents of any thereof (including the Railroad Company), as may be approved by the Interstate Commerce Commission and the Court in the Reorganization Proceeding pursuant to said Section 77.

Dated as of January 1, 1937.

[Endorsed]: Filed with Interstate Commerce Commission Sep. 28, 1936. Filed with Clerk May 26, 1937. [158]

Before the  
Interstate Commerce Commission

Finance Docket No. 10913

In the Matter of

The Western Pacific Railroad Company,  
Debtor,

PLAN OF REORGANIZATION FOR THE  
WESTERN PACIFIC RAILROAD COM-  
PANY, PROPOSED BY A. C. JAMES CO.,  
A JUNIOR CREDITOR.

The following outline Plan of Reorganization for The Western Pacific Railroad Company is submitted by A. C. James Co., an intervening junior creditor, to the Interstate Commerce Commission, for consideration by the Commission.

A. Basic principles upon which proposed Plan of Reorganization is constructed.

It is submitted that a sound plan for the readjustment of the capital structure of The Western Pacific Railroad Company. (hereinafter called the "Railroad Company"), should meet the following standards:

(1) It should provide for the securing of new money, presently required, on the most economical basis; [161]

(2) It should furnish vehicles for financing future capital requirements on a sound basis;

(3) It should preserve, so far as possible, the simplicity of the present capital structure of the Railroad Company;

(4) In view of the favorable ratio of property valuation to present debt,\* it should preserve present debt as debt;

(5) It should refrain from capitalizing unearned and unpaid interest, as a permanent part of the capital structure; and

(6) Necessarily, it should so reduce fixed charges as to render unlikely the recurrence of the present difficulties of the Railroad Company, even though we again pass through a pe-

---

\*Interstate Commerce Commission valuation of the physical property of the Western Pacific System, plus additions at cost to present time, is approximately \$145,000,000 and total funded debt of Railroad Company (exclusive of holding company open account advances and accrued interest) is approximately \$63,000,000, or less than 44% of the property valuation.



riod in which business conditions are comparable with those of the past seven years.

B. General comments as to proposed Plan of Reorganization.

It is recommended that no new corporation be substituted for the Railroad Company, to effect the proposed capital readjustments, as it is believed the powers vested in the Interstate Commerce Commission and the Courts under Section 77 of the Bankruptcy Law are adequate to accomplish the necessary changes in capital structure without substitution of a new corporation.

The amounts of existing indebtedness are stated as of July 1, 1936, and in no case is reference made to interest accrued and unpaid thereon, as it is definitely proposed [162] that such unearned and unpaid interest be not capitalized in any form. Current liabilities of the Railroad Company or the Trustees, and executory leases and other similar contracts are not mentioned, and it is assumed they will be preserved as current obligations of the enterprise.

It is proposed that the Plan be put into effect on January 1, 1937.

C. Proposed provision for new money and necessary modifications in existing capital structure.

1. New Money required by enterprise \$10,000,000

Upon the record heretofore presented to the Commission in this proceeding, it appears that the

Railroad Company presently requires approximately \$10,000,000 of new money for capital purposes (aside from equipment needs, to be financed under equipment trusts, and minor capital requirements for which provision can be made from current earnings). The Trustees of the Railroad Company, appointed in the Section 77 proceeding, have already secured temporarily \$3,000,000 of such new money upon their Trustees' Certificates, and propose shortly to secure an additional \$3,700,000 in like manner.

It is here proposed that the entire \$10,000,000 of required new money be represented by First Mortgage 4% Bonds, secured by a new mortgage which shall be a direct first lien on the railroad.

This new mortgage is intended to furnish the vehicle for future senior financing.

The \$10,000,000 of First Mortgage 4% Bonds, presently to be sold, shall first be offered directly to the stockholders of The Western Pacific Railroad Corporation (the Delaware holding company, which, at present, [168] holds all the preferred and common stock of the Railroad Company) with a bonus at the rate of 15 shares of Common Stock, of \$100 par value, of the Railroad Company for each \$1,000 First Mortgage Bond purchased.

It is proposed that the entire \$10,000,000 of new money so raised shall be used for the rehabilitation program now under way, or for subsequent additions and betterments, and no part of it is to be

set aside as a reserve fund to provide for fixed charges or operating expenses.

2. Existing Equipment Trusts, Baldwin lease and Pullman contracts \$2,048,190.

These are to remain undisturbed. It should be borne in mind that additional equipment trust obligations will probably be created in the near future to provide the necessary motive power and rolling stock.

3. Present First Mortgage Bonds \$49,290,100.

These bonds are to be refunded into a like principal amount of General Mortgage 4% Income Bonds, having a lien junior to the First Mortgage Bonds described under Subdivision 1 above. Each present First Mortgage bondholder is to receive for each \$1,000 bond now held, \$1,000 principal amount of General Mortgage 4% Income Bonds, together with a bonus of five shares of Common Stock of the Railroad Company, of \$100 par value.

4. Secured Notes of Junior Creditors \$10,450,263

These obligations represent advances made by Reconstruction Finance Corporation, Railroad Credit Corporation and A. C. James Co., during the depression, and accrued to the benefit of the First Mortgage bondholders, either by (1) paying charges which were liens prior to the First Mortgage lien, or (2) paying un- [164] earned interest on the First Mortgage bonds, or (3) being directly applied to the construction of income producing property, which is an essential part of the railroad.

These Secured Notes are supported by the pledge of General and Refunding Bonds of the Railroad Company in the principal amount of \$18,999,500. These bonds are all the bonds issued under the General and Refunding Mortgage of January 1, 1932. These bonds are held, as between the three junior creditors, in varying ratios, to the amounts of the actual advances, but in each case solely as collateral.

It is proposed that the Secured Notes be refunded into Four Percent. Convertible Debentures, in like principal amount, together with a bonus of five shares of Common Stock of the Railroad Company, for each \$1,000 of Secured Notes so refunded, and the collateral held by the junior creditors surrendered and cancelled.

5. Advances on Open Account \$5,807,650

These advances, made by The Western Pacific Railroad Corporation, the Delaware holding company, as to \$5,757,650.30 principal amount, and by Western Realty Company, a subsidiary of The Western Pacific Railroad Corporation, as to \$50,000, are to be refunded into 6% Preferred Stock of the Railroad Company, on a dollar for dollar basis.

6. Present 6% Preferred Stock \$28,300,000

All of this is now held by The Western Pacific Railroad Corporation, the present Delaware holding company. Under this Plan, the Preferred Stock is to be delivered to the Railroad Company, and,

to the extent of \$5,807,650 used to refund the Advances on Open Account referred to in Subdivision 5 above; to the extent of \$15,675,395 held in the Treasury of the Railroad Company against the possible exercise of conversion rights by the holders of the Four Percent Convertible Debentures mentioned under Subdivision 4 above; and the balance \$6,816,955 used, from time to time, with the approval of the Commission, to provide a vehicle for junior financing of future capital needs of the Railroad Company.

7. Common Stock \$47,500,000

All of this Common Stock is now held by The Western Pacific Railroad Corporation, the present Delaware holding company. Of this total, \$24,645,050 will be given to the present First Mortgage bondholders as a bonus with the General Mortgage 4% Income Bonds, which they are to receive in exchange for their present debt, and \$5,225,132 as a like bonus, to the junior creditors, with the Four Percent Convertible Debentures, which they are to receive in exchange for their present debt. Of the balance, \$15,000,000 will be given as a bonus with the new First Mortgage 4% Bonds, to be issued for the new money, and offered to the existing stockholders of the Delaware holding company. The balance of \$2,629,818 is to be delivered to the Reorganization Committee, constituted as hereinafter provided, and to be used by the Reorganization Committee, with the approval of the Commission,



for (a) compensation of underwriters of the First Mortgage 4% Bonds, if such underwriting shall be deemed necessary, (b) compensation of the Reorganization Committee, and (c) to the extent not so used, cancelled. [166]

D. Description of new securities.

1. First Mortgage 4% Bonds

The new First Mortgage is to be a direct first lien upon the railroad and other fixed property and equipment (subject, of course, to equipment trust priorities), of the Railroad Company, and to be further secured by a pledge of the entire interest of the Railroad Company in its subsidiary feeders.

It is proposed that the new First Mortgage shall be an open end mortgage, under which additional series, differing as to date of maturity and interest rate, but with equal lien, may be issued from time to time with the approval of the Commission, to provide for additions, betterments, improvements or extensions, in principal amounts, from time to time, not in excess of 75% of the actual cost of the specific additions, betterments, improvements or extensions which are the basis of the particular issue.

In the event it is deemed advisable by the Reorganization Committee, with the approval of the Commission, to limit the principal amount of said First Mortgage 4% Bonds which may ultimately be issued; then it is suggested that such limitation be fixed at \$50,000,000.

The \$10,000,000 principal amount of First Mortgage 4% Bonds, presently to be issued under this Plan, are to be dated January 1, 1937, to mature January 1, 1967, and to bear 4% interest, unless in the opinion of the Reorganization Committee, approved by the Commission, a higher rate of interest shall be required, at the time of such issue, to insure the raising of the necessary new money.

The First Mortgage 4% Bonds, presently to be issued, and subsequent series of bonds to be issued from time to time, under the First Mortgage, shall contain ap- [167] propriate provisions for redemption, in whole or part, prior to maturity, at their principal amount and accrued interest, with such premium or premiums as may be determined from time to time, and approved by the Commission.

## 2. General Mortgage 4% Income Bonds

The General Mortgage shall be a lien on all the property covered by the First Mortgage, subject only to the lien of the First Mortgage. The bonds to be issued under the General Mortgage are to be limited to \$49,290,100 and are to be exchanged, dollar for dollar, for the present First Mortgage Bonds of the Railroad Company.

The General Mortgage Income Bonds are to be dated January 1, 1937, are to mature January 1, 1987, and are to bear interest at the rate of 4% per annum, payable only out of Available Net Income, as herein defined.

Under the terms of said General Mortgage, Available Net Income shall be determined for each

period of six months ending June 30 or December 31 (hereinafter called "Income Period"), beginning with the Income Period ending June 30, 1937. Available Net Income for any Income Period shall be determined by deducting from income of the Railroad Company available for fixed charges for such Income Period (determined in accordance with accounting rules of the Interstate Commerce Commission), all interest charges on equipment trusts and equipment leases, and all interest charges on the First Mortgage 4% Bonds.

Interest on General Mortgage 4% Income Bonds shall be paid only in amounts equal to one-fourth of 1% or multiples thereof; smaller fractional amounts being carried forward and added to that portion of the Available Net Income for the next succeeding income period required to be applied to the payment of interest on such bonds. Except insofar as such smaller fractional amounts are carried forward, as hereinabove provided, such interest payments are to be non-cumulative.

General Mortgage 4% Income Bonds are to be redeemable in whole or part, upon thirty days' notice on any interest payment date, at their principal amount, together with any interest thereon payable on said date, out of Available Net Income, as hereinabove defined.

### 3. Four Percent. Convertible Debentures

The Four Percent. Convertible Debentures are to be issued in the amount of \$10,450,263 to the pres-

ent junior creditors of the Railroad Company in exchange for the Secured Notes now held by those creditors dollar for dollar (the collateral held by the junior creditors being surrendered and cancelled at the time of such exchange) and such debentures are to be limited to the amount necessary for such exchange with the junior creditors.

These Four Percent. Convertible Debentures are to be dated January 1, 1937, and to mature January 1, 1957, and are to bear interest at the rate of 4% per annum, payable only out of Available Net Income, after interest payments at the rate of 4% per annum shall have been made, or provided for, on the General Mortgage 4% Income Bonds. Interest on these Four Percent. Convertible Debentures is to be non-cumulative.

The Four Percent. Convertible Debentures are by their terms, to be convertible, at any time before the actual call and retirement of such debentures into 15 shares of 6% Preferred Stock of the Railroad Company, at \$100 par value for each \$1,000 principal amount of convertible debentures. [169]

#### E. Formation of Reorganization Committee.

To facilitate the definitive formulation and submission to security holders of this Plan, if it shall be approved by the Commission, it is proposed that there be organized a Reorganization Committee, consisting of five members. Subject to the approval of the Commission, one member of this Reorganization Committee shall be nominated by the Institu-

tional Bondholders' Committee, one by the Commission, to represent other First Mortgage bondholders, one by the junior creditors as a group, one by The Western Pacific Railroad Corporation, to represent the present equity owners, and one by the United States District Court for the Northern District of California, Southern Division, to represent the public served by the Railroad Company.

Subject to the approval of the Commission, said Reorganization Committee shall, in its discretion, determine the method of carrying out the Plan, the form, and except as herein otherwise expressly provided, the terms and provisions of all mortgages, debenture agreements, bonds, debentures, coupons, purchase warrants, subscription warrants, acceptances, assents, and all other instruments necessary or convenient for the carrying out of the Plan.

The Committee may act by a majority of its members as from time to time constituted, at a meeting or in writing without a meeting. The Committee may employ such agents, attorneys and others as it may deem desirable for the purposes of the Plan. The Committee may from time to time delegate to others any power or discretion conferred upon it by the Plan; and the members of the Committee shall not be liable for any action taken by them in good faith or by any person employed by the Committee in good faith, or for other acts or [170] omissions, except for their respective individual malfeasance or neglect.



The Committee may from time to time, whether before or after acceptance of the Plan by the holders of securities, modify the Plan, in accordance with, and subject to, the provisions of said Section 77; and the term "Plan" as used herein shall be deemed to include any such modification.

All the expenses of the Committee, when and as approved by the Commission, are to be paid by the Railroad Company. The members of the Reorganization Committee shall be compensated for their services, to the extent the Commission shall approve, in Common Stock of the Railroad Company provided for the purpose as hereinabove set forth.

The Reorganization Committee shall, in its discretion, but subject to the approval of the Commission, make such agreement or agreements for the underwriting of the First Mortgage 4% Bonds of the Railroad Company, presently to be issued under this Plan, as it may deem necessary and advisable, but compensation for such underwriter or underwriters shall be paid solely in Common Stock of the Railroad Company, provided for the purpose as hereinabove set forth.

F. Method of participation in, and consummation of, the Plan.

The Plan shall not be carried out until it shall have been approved by the Commission and the Court in the Reorganization Proceeding, pursuant to the requirements of Section 77 of the Bankruptcy Act, and until it shall have been accepted by two-thirds of the creditors of each class, as the

same may be classified by the Court in the Reorganization Proceeding, and by two-thirds of the stock of each class. [171]

G. Expenses of the Plan.

Subject to the approval of the Commission, all expenses of the Plan, and all costs of administration and other allowances made by the Court in the Reorganization Proceeding, shall be paid by the Railroad Company, from its current cash balances, at the time the Plan is made effective.

Dated October 26, 1936. [172]

**SCHEDULE A**

**PRESENT CAPITAL LIABILITIES**

(Stated as of July 1, 1936, and exclusive of unpaid interest)

	Principal	Fixed Charges
Equipment Trusts, Baldwin Lease and Pullman Contract .....	\$ 2,048,190	\$ 86,473
First Mortgage 5% Bonds, due 1946 .....	48,290,100	2,464,505
Secured Notes:		
Reconstruction Finance Corporation \$2,963,000		
Railroad Credit Corporation .....	2,487,463	
A. C. James Co. ....	4,999,800	10,450,263
		435,072
Open account debt to affiliated companies .....	5,807,650	290,382
Preferred Stock .....	28,300,000	
Common Stock .....	47,500,000	
Totals .....	\$143,396,203	\$3,276,432

\*No reference is made above to General and Refunding Mortgage 5% Bonds of the Railroad Company, which are outstanding solely as collateral to the Secured Notes.

[173]

## SCHEDULE B

### PROPOSED NEW CAPITALIZATION

(As of January 1, 1937)

	Principal	Fixed Charges	Contingent Interest
Undisturbed Equipment Trusts, Baldwin Lease and Pullman Contract.....	\$ 2,048,190	\$ 86,473	
First Mortgage 4% Bonds.....	10,000,000	400,000	
General Mortgage 4% Income Bonds.....	49,290,100		\$1,971,604
Four Percent. Convertible Debentures.....	10,450,263		418,011
Preferred Stock (Balance held in Treasury of Railroad Company.....)	5,807,650		
Common Stock:			
Bonus to present First Mortgage bondholders.....	\$24,645,050		
Bonus to present junior creditors.....	5,225,132		
Bonus to purchasers of new First Mortgage 4% bonds.....	15,000,000		
Available for use under Plan.....	2,629,818	47,500,000	
<b>Totals.....</b>	<b>\$125,096,203*</b>	<b>\$486,473</b>	<b>\$2,389,615</b>

\*This should be compared with the Interstate Commerce Commission valuation of property of Railroad System, including additions to date, amounting to approximately \$145,000,000.

[Endorsed]: May 26, 1937. [174]

## Interstate Commerce Commission

Finance Docket No. 10913

The Western Pacific Railroad Company  
Reorganization

Submitted

Decided

Plan of reorganization of the Western Pacific Railroad Company, pursuant to section 77 of the Bankruptcy Act, as amended, recommended.

Frank C. Nicodemus, Jr., for The Western Pacific Railroad Company.

Robert E. Coulson for A. C. James Company.

James B. Alley, C. C. McChord, and C. M. Clay for Reconstruction Finance Corporation.

Daniel Willard, Jr., for Railroad Credit Corporation.

Robert T. Swaine for Institutional Bondholders Committee.

Orville W. Wood for Crocker First National Bank of San Francisco and Samuel Armstrong.

H. C. McCollom and Orrin G. Judd for Irving Trust Company.

PROPOSED REPORT OF THE BUREAU  
OF FINANCE

The Western Pacific Railroad Company, hereinafter called the debtor, on August 2, 1935, filed a petition in the District Court of the United States for the Northern District of California, Southern

Division, stating that it was unable to meet its debts as they matured and that it desired to effect a plan of reorganization under the provisions of section 77 of the act of July 1, 1898, entitled "An Act to Establish a Uniform System of Bankruptcy Throughout the United States," as amended. The court, on the same day, made and entered an order approving the petition as properly filed and, among other things, authorizing and directing the debtor, pending further order of the court, to operate and maintain the railroad and property of the debtor and to manage and conduct the debtor's business as a railroad company. Trustees were appointed on September 23, 1935, and their appointments were ratified by the Commission on October 30, 1935. Copies of the debtor's petition and the order thereon have [175] been transmitted to the Commission by the clerk of the court; and in like manner the Commission has received lists of all known creditors and stockholders of the debtor, and copies of the orders of the court determining the time within which the claim of creditors might be filed or evidenced and dividing the creditors and stockholders into classes. These documents and other documents similarly received are now of record in the proceeding before the Commission.

The debtor, on February 8, 1936, filed a plan of reorganization with the court and the Commission. Pursuant to the provisions of section 77(d) of the Bankruptcy Act, the Commission, after due notice, began public hearings upon the debtor's plan of re-



organization on March 23, 1936. Two other plans for the reorganization of the debtor were filed during the proceedings; one, on behalf of certain institutional bondholders, on September 28, 1936, and the other, on behalf of A. C. James Company, a secured creditor of the debtor, on October 26, 1936. These parties intervened in the proceeding and were represented by counsel at the hearing. Other interveners, similarly represented, included the trustees under the mortgages, the Reconstruction Finance Corporation and the Railroad Credit Corporation, secured creditors. Hearings in this proceeding were completed on December 9, 1936, and briefs were filed on January 11, 1937.

#### Location and General Description of Property

The debtor owns or operates a total of 1207.51 miles of standard-gage, steam railroad. The main lines extend 924.17 miles eastward from Oakland, Calif., to Salt Lake City, Utah, and northward 111.81 miles from Keddie to Bieber, Calif., (with operating rights over the Great Northern Railway 46.38 miles from Bieber to Hambone, Calif.). The debtor also operates 4.2 miles of ferry service from Oakland to San Francisco and 185.30 miles of second [176] main track, of which 182.91 miles between Weso and Alazon, Nevada, are owned by the Southern Pacific. This territory is known as the "Paired Track" district since the two lines are used as a double-track railroad by both companies. Various

branch lines springing from the Oakland-Salt Lake City line are as follows:

Niles to San Jose, Calif.....	23.07 miles
Calpine Junction to Calpine, Calif.....	12.62 "
Hawley to Loyalton, Calif.....	12.79 "
Reno Junction to Reno, Nevada.....	33.11 "
Burmaster to Warner, Utah.....	15.52 "
Miscellaneous .....	21.79 "
<hr/>	
Total.....	118.90 miles

### Owned or Controlled and Jointly Affiliated Railroad Companies

The debtor owns all the outstanding capital stock of Sacramento Northern Railway, an electrically operated standard-gage, freight and passenger railroad aggregating 276.2 miles of road serving and connecting San Francisco and Oakland with various Sacramento Valley cities, principally Pittsburg, Vacaville, Sacramento, Woodland, Marysville, Colusa and Oroville, all in California.

By ownership of more than 99 per cent of the outstanding capital stock, the debtor controls the Tidewater Southern Railway which operates a standard-gage, steam freight line aggregating 61.38 miles of road connecting Stockton with Manteca, Escalon, Modesto and Turlock in the San Joaquin Valley of California.

The debtor owns all the outstanding capital stock of the Deep Creek Railroad Company, which owns and operates a standard-gage, steam railroad from Wendover to Gold Hill, Nevada, a distance of 44.6 miles. In addition it owns 50 per cent of the capital

stock of The Salt Lake City Union Depot and Railroad Company; 33 $\frac{1}{3}$  per cent of the capital stock of the Central California Traction Company, operating an electrically operated freight railroad from Stockton to Sacramento, Calif., with a road mileage of 53.78 miles; and 50 per cent of the capital stock of the Alameda Belt Line, [177] operating 15.86 miles of terminal switching line in the city of Alameda on the San Francisco Bay.

None of the above subsidiary or affiliated companies have filed a petition under Section 77 of the Bankruptcy Act.

#### Corporate and Financial History

The debtor was incorporated under California laws on June 16, 1916, and as of July 14, 1916, succeeded to the railroads, properties, etc., of The Western Pacific Railway Company sold at foreclosure on June 28, 1916. Upon incorporation, the debtor had an authorized capital stock of \$75,000,000 consisting of 475,000 shares of common and 275,000 shares of preferred stock of the par value of \$100 each.

The debtor by its first mortgage dated June 26, 1916, to the First Federal Trust Company and Henry E. Cooper, trustees, (Crocker First National Bank, of San Francisco, and Samuel Armstrong, now successor trustees) authorized a maximum of \$50,000,000 of first mortgage bonds at any one time outstanding. A principal amount of \$20,000,000 thereof was issued and sold after its organization

and as a part of the plan of reorganization. These bonds were sold at 90 and realized \$18,000,000 in cash. Of this amount, approximately \$2,000,000, together with cash from receivers, was applied in defraying expenses of incorporation, expenses incurred in connection with foreclosure and reorganization proceedings, payment of distributive shares of non-participating first mortgage bondholders of the old company; and \$1,000,000 was retained as working capital. The balance of approximately \$15,000,000 was deposited under the debtor's first mortgage and applied to capital purposes as provided in the mortgage.

The debtor thus commenced operations with \$75,000,000 par value of capital stock issued and outstanding, and \$20,000,000 of [178] its first mortgage bonds outstanding. Additional bonds were not issued by the debtor until 1921, in which year \$4,180,000 of its first mortgage bonds were sold at 85 and the \$3,553,000 realized was used to purchase properties of the Sacramento Northern Railroad through the Sacramento Northern Railway. As of September 30, 1936, a total of \$49,290,100 face amount of the debtor's first mortgage bonds were outstanding, the additional bonds having been issued for the following purposes: \$3,000,000 in 1922 to retire outstanding equipment trust certificates; \$4,000,000 in 1925 for general capital purposes; \$2,600,000 in 1926 for general capital purposes; \$2,950,000 in 1927 in substitution of the \$3,000,000 issued in 1922 then outstanding in the aggregate

amount of \$2,950,000; \$5,000,000 in 1929 for general capital purposes; \$572,800 in 1930 for purchase of San Francisco & Railroad Company properties through Sacramento Northern Railway; \$5,000,000 in 1930 for general capital purposes of debtor and of subsidiary, Sacramento Northern Railway; \$5,000,000 in 1931 and 1932 to finance in part construction and/or acquisition of Northern California Extension; and \$645,000 in 1931 for general capital purposes. Interest on the bonds was paid on the semi-annual interest payment dates until March 1, 1934. The interest payment due on that date was not paid, and no interest payment has since been made.

Since its organization the debtor has created equipment trust obligations in the total amount of \$13,400,000; there being \$1,930,000 face amount of such obligations outstanding as of September 30, 1936, and on that date there also remained unpaid on a conditional sale lease of locomotives \$314,665. All interest and principal payments on equipment trusts and conditional sale lease have been met.

[179]

The debtor, in addition to the \$5,000,000 of its first mortgage bonds, issued in 1931 and 1932, \$5,000,000 of gold debentures to finance the cost of its Northern California Extension. These debentures were retired in 1932 through the issue of notes payable to A. C. James Co., for \$4,999,800 (\$200 being paid in cash), which notes were secured by \$6,249,-



500 face amount of the debtor's general and refunding mortgage, series "A", 5 per cent gold bonds. The latter bonds were issued under the debtor's general and refunding mortgage, dated January 1, 1932, The Chase National Bank of the City of New York, trustee, authorizing a maximum of \$100,000,000 of general and refunding bonds to be at any one time outstanding, but reserving \$49,292,300 principal amount thereof for the purpose of refunding, paying, purchasing, redeeming or otherwise acquiring the first mortgage bonds then outstanding in that amount, and reserved \$5,000,000 principal amount thereof against the outstanding debentures. The reserved bonds were issuable upon the retirement of the securities against which they were reserved.

None of the debtor's general and refunding bonds have been sold; but \$18,999,500 principal amount have been nominally issued and are nominally outstanding solely as collateral to secure certain of the debtor's promissory notes. In November, 1936, The Chase National Bank resigned as trustee of the mortgage and the Irving Trust Company of New York City, was appointed successor trustee.

### Present Financial Structure

The trustees' balance sheet as of November 30, 1916, shows total assets of \$171,096,992.80. Investments included therein total \$160,868,348.32. Of total investments, road and equipment amounts to \$139,371,768.08; sinking fund and deposits, \$124,-

155.96; and miscellaneous physical property \$3,670,041.32. Investments in affiliated companies pledged under the debtor's first mortgage [180] amount to \$10,224,421.66 and consist of \$99,500.40 for capital stock of The Salt Lake City Union Depot and Railroad Co., \$999,500.00 for capital stock of Sacramento Northern Railway, \$450,000.00 for capital stock of Deep Creek Railroad Company, \$175,220.75 for capital stock of Standard Realty and Development Company, \$3,975,456.13 for Sacramento Northern Railroad 5 per cent twenty year gold bonds, and \$4,524,744.38 notes receivable from Sacramento Northern Railway. Investments in affiliated companies pledged under the debtor's general and refunding mortgage amount to \$3,159,061.78, and consist of \$1,223,848.94 capital stock of Tidewater Southern Railway Company, \$128,651.56 common stock, \$264,715.47 preferred stock and \$270,375.50 first mortgage 5 per cent gold bonds of Central California Traction Company, \$1,318.63 capital stock of other companies, and \$804,551.68 notes receivable from Tidewater Southern Railway Company, Standard Realty and Development Company, and Deep Creek Railroad Company. Investments in affiliated companies unpledged amount to \$4,240,257.27, and consist of \$3,405,356.42 advances to Sacramento Northern Railway, \$770,834.73 advances to other affiliated companies, \$5,500.00 capital stock of Alameda Belt Line, and \$58,566.12 due from The Railroad Credit Corporation. Other investments amount to \$78,678.25, and consist principally of

\$74,472.88 advances to Railway Equipment and Realty Co. Ltd.

Current assets are shown in the amount of \$7,653,809.28, and comprise \$3,290,601.55 cash, \$4,722.28 special deposits, \$176,241.25 traffic and car service balances receivable, \$189,208.77 net balances receivable from agents and conductors, \$814,321.64 miscellaneous accounts receivable, \$2,113,166.60 materials and supplies, \$1,054,447.57 interest receivable from affiliated companies, and other current assets of \$10,099.62. Of the \$1,054,447.57 interest receivable, \$369,287.81 is accrued interest [181] on Sacramento Northern Railroad bonds, \$420,729.87 is accrued interest on Sacramento Northern Railway notes receivable, \$224,453.74 is accrued interest on Sacramento Northern Railway advances, and the remainder accrued interest on advances to other affiliates and notes receivable.

Deferred assets are shown in the amount of \$141,222.55 and unadjusted debits in the amount of \$2,433,612.65. The latter item consists of \$24,516.77 rents and insurance premiums paid in advance, \$1,266,699.29 discount on funded debt, and other unadjusted debits \$1,142,396.59.

Liabilities shown on the balance sheet of the same date are capital stock, \$75,800,000.00 consisting of \$47,500,000.00 common and \$28,300,000.00 preferred stock. Total long-term debt is shown in the amount of \$69,476,379.26. Included therein is \$59,504,805.56 funded debt unmaturred, consisting of \$49,290,100.00 first mortgage 5 per cent gold bonds, \$4,999,800.00

notes payable to A. C. James Company, \$2,963,000.00 notes payable to Reconstruction Finance Corporation, \$314,665.00 Baldwin Locomotive Works locomotive lease, \$80,240.56 The Pullman Company—purchase of lounge cars, and \$1,857,000.00 equipment trust certificates. There is also included in long-term debt \$3,000,000.00 trustee's certificates, and \$6,971,573.70 non-negotiable debt to affiliated companies, of which latter amount \$6,915,115.37 is due The Western Pacific Railroad Corporation.

Total current liabilities are shown in the amount of \$14,288,810.44. Included therein are \$2,452,875.24 loans and bills payable, consisting of notes payable to the Railroad Credit Corporation, \$849,649.23 traffic and car service balances payable, \$1,159,297.40 audited accounts and wages payable, \$278,729.95 miscellaneous accounts payable, of which \$203,450.09 are United States [182] Federal Retirement tax employees deduction, and \$8,606,565.43 interest matured unpaid. The latter amount consists of \$97,069.29 interest on The Railroad Credit Corporation notes, \$406,988.88 interest on Reconstruction Finance Corporation notes, \$687,472.50 interest on A. C. James Co. notes, \$18,590.00 interest on equipment trust certificates, and \$7,396,444.78 interest on first mortgage 5 per cent gold bonds. There are also included in the total current liabilities \$761,834.34 accrued unmatured interest, \$2,079.16 accrued unmatured rents, and \$177,749.69 other current liabilities.

Total deferred liabilities are shown in the amount of \$1,153.68, and total unadjusted credits in the amount of \$11,643,121.37. The latter amount is comprised of \$479,026.00 tax liability, \$11,053,713.23 accrued depreciation on equipment, and \$110,382.14 other unadjusted credits.

The liabilities above mentioned amount to a total of \$171,209,464.75. Two additional items totaling \$7,171,169.07, described as surplus-investment in road equipment and cash materials and other property purchased, representing value of Western Pacific Railway property purchased in excess of cash paid and for value of capital stock issued in exchange for same, are shown also on the liability side of the balance sheet. This amount added to the figure of \$171,209,464.75 produces an amount of \$178,380,633.82.

The balance sheet shows a deficit of \$7,283,641.02 in corporate surplus. This consists of appropriated surplus amounting to \$12,072,584.18, represented principally by additions to property through income and surplus and an accumulated debit balance in profit and loss of \$19,356,225.20.

### Rehabilitation Program

By reports and orders of March 5, and October 15, 1936, and January 25, 1937, the Commission granted authority to the debtor's [183] trustees to issue not exceeding \$6,700,000 of trustee's certificates and to assume obligation and liability in respect of not exceeding \$2,320,000 of equipment-trust



certificates: 212 I.C.C. 356, 217 I.C.C. 393, 217 I.C.C. 395, 217 I.C.C. 777. The proceeds from the sale of those securities were to be used in the rehabilitation and improvement of the debtor's fixed plan and existing motive power and cars, and the acquisition of additional equipment. Studies by the debtor, the Reconstruction Finance Corporation and the bondholders' committee show the necessity of expending approximately \$13,375,906 over a period of three years for such purposes in order to place the debtor in proper physical condition to meet the reasonable requirements of existing and future traffic. Under authority of the court, the trustees have initiated the rehabilitation program and it is well under way.

The debtor estimates that \$9,500,000 of new money, exclusive of the \$2,320,000 of equipment-trust certificates, will be required by the reorganized company for the purpose of retiring outstanding trustees' certificates and completing the rehabilitation of the debtor's property. The necessary new money is to be raised by the sale of bonds by the reorganized company.

Under the Commission's accounting rules a part of the rehabilitation expenditures is chargeable to operating expenses. The trustee's report that \$1,585,530 of the rehabilitation expenditures were included in the debtor's operating expenses for 1936. The inclusion of these extraordinary expenses with the debtor's normal expenses obviously reduces the showing of net income available for interest and other charges in that year.

3

### Traffic and Revenue

The main line of the debtor's railroad extending from Oakland, Calif., to Salt Lake City, Utah, forms an important part of a through [184] route from the Pacific Coast to Chicago, Illinois, and other important Middle Western points. Fast through schedules are maintained by the debtor and the Denver & Rio Grande Western Railroad and Missouri Pacific Railroad Company, with which companies the debtor has close affiliations. Its line also connects with the Atchison, Topeka & Santa Fe Railroad at Stockton, Calif., and with the Great Northern Railroad Company at Bieber, Calif., thus forming a link in a north and south route on the Pacific Coast. The latter route is comparatively new, having been established by the extension of the debtor's line northward from Keddle to Bieber, known as the Northern California Extension, and the extension of the line of the Great Northern southward from Klamath Falls, Oregon, to Bieber in the latter part of 1931.

Although operations over the debtor's Northern California Extension commenced in the depth of the depression considerable traffic has moved over it from the start. Traffic over this extension and revenue derived therefrom is, therefore, considered separately from the debtor's other traffic and revenues. During the years 1924 to 1929, inclusive, the debtor and its subsidiary, Sacramento Northern Railway, had an agreement with the Southern Pacific Company for the transportation for the South-

ern Pacific of Certain carload traffic between Chico, Calif., and Weso, Nevada, for \$60 per car, of which the debtor received \$54 per car. This agreement was terminated at the end of 1929, and since the tonnage moved under this agreement and the revenue therefrom was quite large, the statistical data shown below relating to the debtor's traffic have been adjusted by excluding the freight moved under that agreement.

Freight traffic handled and freight revenue received by the [185] debtor for the years 1923 to 1935, inclusive, excluding traffic and revenue under the Chico-Weso Bridge agreement and via Northern California Extension, was as follows:

Year	Cars	Tons	Revenue	Revenue Per Ton	Percent of Increase or Decrease Over or Under Preceding Year	
					Tons	Revenue
1923	96,531	2,875,108	\$10,513,455	\$3.66	—	—
1924	98,297	2,854,602	10,562,340	3.69	-0.7	-0.5
1925	113,633	3,198,214	11,736,434	3.67	+12.0	+11.1
1926	120,545	3,326,637	12,252,189	3.68	+4.0	+4.4
1927	121,071	3,486,668	12,697,985	3.64	+4.8	+3.6
1928	124,110	3,567,798	13,887,953	3.89	+2.3	+9.4
1929	124,181	3,616,927	14,287,250	3.95	+1.4	+2.9
1930	131,242	3,776,046	13,796,125	3.65	+4.4	-3.4
1931	106,321	3,070,577	\$1,078,891	3.61	-18.7	-19.7
1932	83,549	2,330,505	8,558,209	3.67	-24.1	-22.8
1933	83,957	2,359,810	8,520,315	3.61	+1.3	-0.4
1934	93,115	2,616,182	9,173,115	3.51	+10.9	+7.7
1935	92,902	2,489,273	9,910,386	3.98	-4.9	+8.0

Agricultural and manufactured and miscellaneous products comprised the greater part of the traffic moving over the debtor's line from Salt Lake City

to Oakland. In the period 1928 to 1935, inclusive, for example, of the total loads of commodities carried, manufactured and miscellaneous products constituted  $33\frac{1}{3}$  percent, and agricultural products  $33\frac{1}{3}$  percent. Forest products accounted for  $7\frac{1}{2}$  percent, mineral products  $19\frac{2}{3}$  percent, and animal products 6 percent. Of the total freight revenue received from the transportation of this freight, approximately 40 percent was derived from manufactured products, 28 percent from agricultural products, 5 percent from forest products,  $13\frac{1}{2}$  percent from mineral products,  $5\frac{2}{3}$  percent from animal products, and the remainder from L.C.L. freight.

The above tabulation shows that the debtor's freight traffic for 1930, amounting to 3,776,046 tons, was the greatest for any of the years. It moved an average of 2,573,269 tons in the following five years, 1931-1935, inclusive, a decrease of 32 percent as [186] compared with 1930. During the same period, agricultural products transported declined an average of 20 percent, animal products 16.7 percent, mineral products 42.2 percent, forest products 44.4 percent, manufactured products 28 percent, and L.C.L. freight 29.7 percent as compared with 1930.

Freight carried in 1935 amounted to 2,489,273 tons, a decrease of 35 percent under 1930. In 1935, traffic in agricultural products declined 25.1 percent, animal products 27.9 percent, mineral products 51.4 percent, forest products 45.6 percent, manufactured products 20.6 percent, and L.C.L. freight 20.8 percent under 1930.

Revenue from freight in 1930 amounted to \$13,796,125. During the period 1931-1935, inclusive, freight revenue averaged \$9,448,183, a decline of 32.3 percent as compared with 1930. In the same period revenue from agricultural products declined an average of 29.3 percent, animal products 20.8 percent, mineral products 60.9 percent, manufactured products 31.1 percent, and L.C.L. freight 28.2 percent.

Freight revenue amounted to \$9,910,386 in 1935, a decrease of 28.9 percent as compared with 1930. In 1935, revenue received from agricultural products decreased 28 percent, animal products 34.7 percent, mineral products 43.4 percent, forest products 40.3 percent, manufactured products 19.6 percent, and L.C.L. freight 37.2 percent under 1930.

Forty-three percent or 1,637,984 tons of the debtor's freight traffic in 1930 consisted of traffic interchanged with the Denver & Rio Grande Western, Oregon Short Line and Union Pacific. During the period 1931-1935, inclusive, traffic interchanged with those lines averaged 1,196,971 tons, or a decrease of 20 percent under 1930. For the year 1935, traffic interchanged with the same lines amounted to 1,381,186 tons, or a decrease of 15 percent under 1930. [187] It should be noted also that for many years the debtor was dependent upon connections for the greater part of its traffic, and although to a less degree than formerly, it still receives more than one-half of its total freight from connecting car-



riers, and approximately one-third of it is received from and delivered to connections.

The debtor estimates that revenue from freight moving over its line from Oakland to Salt Lake City will amount to \$10,084,951 in 1936, \$10,857,252 in 1937, \$11,629,553 in 1938, \$12,518,672 in 1939, and \$13,747,996 in 1940. The latter amount is an increase of \$3,837,610, or 38.7 percent, over 1935 revenue, and approximately equals that received in 1930.

Freight moved over the Northern California extension in 1932 amounted to 340,107 tons, and \$1,098,616 revenue was derived therefrom. For the year 1933, tonnage and revenue amounted to 396,862 tons and \$1,491,466 revenue, in 1934, to 596,378 tons and \$2,119,427 revenue and in 1935 to 639,980 tons and \$2,289,858 revenue. The principal commodities carried consisted of forest, manufactured and agricultural products. The debtor estimates that revenue from freight moved over this line will amount to \$2,550,524 in 1936, \$2,973,750 in 1937, \$3,406,978 in 1938, \$3,819,559 in 1939, and \$4,171,625 in 1940. The latter amount is an increase of \$1,881,767 or 82 percent over 1935 revenue.

Total revenue to be derived from freight in the period 1936 to 1940, inclusive, is estimated by the debtor to amount to \$12,635,475 in 1936, \$13,831,002 in 1937, \$15,036,531 in 1938, \$16,338,231 in 1939, and \$17,919,621 in 1940. This would be an increase of 3.5 percent in 1936 over 1935, 13.3 percent in 1937, 23.3 percent in 1938, 33.9 percent in 1939, and 46.8 percent in 1940.

A witness for the debtor testified that the increased revenues estimated for the future were based on expected increases in traffic [188] and freight rates. The drastic decline in revenues recently suffered by the debtor, in the opinion of this witness, resulted not only from the past depression but, also, to intense competition from water and motor carriers.

The debtor and other lines with which it has a joint freight rate arrangement have water competition on transcontinental traffic via the Panama Canal between the Pacific Coast and Atlantic and Gulf ports, and in connection with canal lines and inland waterways. There is also strong competition coastwise between California and Washington. It was the opinion of the debtor's witness that increased operating expenses would compel water carriers to increase rates and thereby would divert traffic to railroads. The witness also was of the opinion that railroad freight rates as a whole are as low today as they will be for a number of years, and the tendency in the immediate future will be towards a higher level of rates.

This witness stated that prior to the advent of motor truck competition, practically all the debtor's traffic between California and Utah moved under class rates, which for the first four classes were \$2.16 $\frac{1}{2}$ , \$1.84 $\frac{1}{2}$ , \$1.62 $\frac{1}{2}$  and \$1.35 per 100 pounds between San Francisco and Utah common points. Motor truck competition made it necessary for the debtor to publish pick-up and delivery rates of \$1.00

and \$1.25 per 100 pounds, on a great many commodities, and today at least 90 percent of such traffic of the debtor moves under the reduced rates. It was his opinion that effective regulation of motor carriers would tend to divert traffic to the railroads.

Passenger, mail, express and other related revenues received by the debtor for the years 1923 to 1935, inclusive were as follows:

Year	Revenues	Year	Revenues
1923	\$3,250,677	1929	\$2,135,828
1924	2,891,137	1930	1,738,881
1925	2,697,899	1931	1,288,093
1926	2,515,900	1932	645,760
1927	2,350,320	1933	433,959
1928	2,217,421	1934	457,481
		1935	559,816
			[189]

It thus appears that such revenues steadily declined from 1923 to 1934, the decrease amounting to 79.7 percent in 1933 under 1923. In 1935 such revenues had increased 22.5 percent over 1933, but were still 73.8 percent below those for 1923. The debtor estimates that revenues from these sources will amount to \$654,710 in 1936, \$1,063,058 in 1937, \$1,299,060 in 1938, \$1,860,815 in 1939, and \$1,535,372 in 1940. A witness for the debtor testified that the debtor expected to inaugurate additional passenger service between San Francisco and Salt Lake City in May, 1937, only one passenger train daily.

between those points having been operated since April 24, 1932. He stated that by reason of shortening of schedules and greater advertising of the improved service of the Denver & Rio Grande Western via the Dotsero Cut-Off, which road with the debtor provides one of the most scenic trips between California and the East, passenger revenues should be materially increased.

The debtor filed a forecast that total railway operating revenues would amount to \$13,438,342 in 1936, \$15,053,934 in 1937, \$16,507,579 in 1938, \$18,383,490 in 1939, and \$19,654,935 in 1940.

As a bridge line to and from the Pacific Coast the debtor's railroad may as a result of the completion of the Dotsero Cut-off in 1934, come into still greater use. The railroad distance between Denver and Salt Lake City and points east of the former and west of the latter is greatly shortened by use of this Dotsero Cut-off and the Denver and Salt Lake's Moffet Tunnel. The rehabilitation program of the debtor's road now in progress and the betterment of its equipment should enable it to give improved service. As a consequence the debtor and the lines with which it is closely affiliated should be in better position to compete with the Southern Pacific and Union Pacific for transcontinental traffic. Increased traffic over its Northern California Extension reasonably may be expected. Greater through and local traffic should result from a further revival in general business conditions. Whether revenues in the future will reach the level estimated by the

debtor in 1940, is open to doubt. To the extent that the debtor relies upon increased freight rates, and a recovery of the traffic lost to competing forms of transportation under present state and federal regulatory conditions, its estimates rest upon [190] uncertainties.

### Traffic and revenue of subsidiaries

The main line of the Sacramento Northern Railway extends from Oakland to Chico, Calif., and both freight and passenger services are rendered over it. Its freight traffic consists largely of agricultural, manufactured and miscellaneous and mineral products.

Freight traffic and revenue derived therefrom for the years 1930 to 1935, inclusive, were as follows:

Year	Tons	Revenue
1930	840,306	\$1,234,696
1931	743,220	971,482
1932	629,792	769,412
1933	649,554	717,435
1934	704,472	760,033
1935	697,464	760,528

A witness for the debtor testified that the decline in traffic was occasioned primarily by competition of motor trucks, depressed economic conditions, and the displacement of coal by oil and natural gas. It was his opinion, however, that the Sacramento Northern's freight earnings in the future should increase quite materially since it was reasonable to expect an improvement in the market demand for



California fruits and vegetables, and that improved facilities recently had been made available to the carrier's shippers. He further testified that general business conditions were improving and that the carrier was in a better position to meet truck competition. The witness was of the opinion that the carrier's gross revenues from transportation and other railway operations would amount to \$1,322,676 in 1936, \$1,417,458 in 1937, \$1,528,492 in 1938, \$1,616,891 in 1939, and \$1,689,038 in 1940. The latter amount is a 38.3 percent increase over gross revenues [191] for 1935, and is approximately \$40,775 greater than the actual gross revenue for 1931, but is approximately \$394,000 less than the actual for 1930.

The main line of the Tidewater Southern Railway extends from Stockton to Hillmar, Calif., serving a territory predominantly agricultural. The carrier's freight traffic consisted principally of agricultural products and manufactured and miscellaneous commodities.

Freight traffic and revenue derived therefrom for the years 1930 to 1935, inclusive, were as follows:

Year	Tons	Revenue
1930	199,607	\$425,506
1931	227,856	264,796
1932	249,820	230,450
1933	255,833	202,434
1934	266,274	271,519
1935	211,264	272,299

A witness for the debtor testified that the Tidewater Southern's total railway operating revenues would amount to \$287,136 in 1936, slightly higher than those in 1935, but that since the small area served by the line does not afford much opportunity for increased acreage production, earnings are not expected to increase materially in the future.

The Deep Creek Railroad Company operates 44.6 miles south from Wendover, Utah, serving a territory devoted principally to mining. Its freight revenues are dependent largely on mining activities in the Gold Hill District at the southerly terminus of the line, although some revenue is derived from the movement of sheep to winter ranges in the fall and out in the spring. [192]

A witness for the debtor testified that the revenues of this line have in the past few years been nominal, but with a revival in mining it is possible for a traffic to develop that would increase materially the revenue. For example, in 1923 revenues were \$42,385, in 1924, \$71,670, and in 1925, \$40,268. In 1934 and 1935, however, they were only \$7,383 and \$5,355, respectively. For the next several years revenues are not expected to increase.

#### Earnings Available for Charges

The reported consolidated net income of the debtor's system available for payment of interest on funded debt for the years 1926-1935, inclusive, was, \$4,759,282 in 1926, \$2,674,494 in 1927, \$2,964,371 in 1928, \$2,529,846 in 1929, \$1,552,487 in 1930, \$186,

708 deficit in 1931, \$252,706 in 1932, \$674,007 in 1933, \$1,084,244 in 1934, and \$805,589 in 1935. Operating ratio percentages for the same years were, respectively, 70.3, 79.2, 80.3, 83.2, 84, 91, 85.8, 83, 81.1, and 83.7.

It would appear, however, that before the foregoing amounts may be considered indicative of future earnings they are subject to adjustment. It was testified, for example, that a substantial amount of deferred maintenance had been permitted to accrue in debtor's property by 1927. Beginning in that year and continuing into 1931, considerable sums were expended yearly in an effort to overcome existing deferred maintenance. It was stated that \$687,605 was so expended in 1927, \$1,305,681 in 1928, \$1,075,330 in 1929, \$711,462 in 1930, and \$122,735 in 1931. This program of rehabilitation was discontinued in 1931 by reason of drastically declining revenues, and it was testified that approximately \$5,000,000 of deferred maintenance still existed in the debtor's property at the end of 1935. Witnesses for the debtor were unable [193] to allocate any specific amount for undermaintenance to any of the years shows above.

It was further pointed out that in arriving at the foregoing figures an average of approximately \$140,000 per annum had been deducted for amortization of bond discount and that deduction would not be required following reorganization.

There also are reflected in the above earnings for the years 1926-1929, inclusive, substantial amounts received by the debtor under the Chico-Weso agreement with the Southern Pacific for movement of Southern Pacific cars, which was terminated at the close of 1929. On the other hand revenues from traffic over the debtor's Northern California Extension are not reflected in the net income available for interest shown for the years 1926-1931, inclusive, and future earnings from that source are not reasonably reflected in the amounts shown for the years 1932 and 1933.

The above amounts do not reflect the effect on future income of taxes under the Social Security Act, approved August 14, 1935, and the Railroad Retirement Act and related Excise Tax Act, approved August 29, 1935, which impose additional taxes upon carriers. It is estimated by the Commission's Bureau of Accounts that the debtor's proportion of such taxes would have amounted to approximately \$537,653 in 1930, \$488,633 in 1931, \$365,498 in 1932, \$331,149 in 1933, and \$257,345 in 1934. While data of record are insufficient to permit accurate mathematical adjustments of the amounts reported available for interest in the years 1926-1935, inclusive, in the light of the above-mentioned factors, it is apparent that such amounts should be considered in determining the debtor's probable future earnings available for interest and dividends.

For the year ended December 31, 1936, total operating revenues of the debtor's system were reported as \$16,547,344 and total [194] operating expenses as \$14,449,275, of which \$1,585,530 was attributed to the debtor's current program of rehabilitation. If these extraordinary expenditures were eliminated, the consolidated net income of the system available for interest on funded debt for the year would be \$1,766,632, instead of \$181,102. For the year 1935 (when no substantial amount of expenditures was made on account of the rehabilitation program) net income available for interest was \$805,589.

In statements filed in this proceeding the debtor has estimated that total operating revenues of its system for the years 1936-1940, inclusive, will be, respectively, \$15,050,200, \$16,761,200, \$18,325,200, \$20,288,200, and \$21,632,200. Excluding operating charges incident to its rehabilitation program, the estimated consolidated income available for interest on funded debt for the same years is respectively, \$1,524,086, \$2,342,586, \$2,929,586, \$3,652,486, and \$4,956,486, or an average of \$2,901,040. Operating ratios estimated for the same years are, respectively, 77.3 per cent, 75.1 per cent, 72.4 per cent, 70.8 per cent, and 69.6 per cent. Expenditures incident to the debtor's rehabilitation program and which normally are chargeable to operating expense under the Commission's accounting rules, are estimated by the debtor at \$1,747,384 in 1936, \$2,021,312 in 1937, and \$1,280,074 in 1938, which sums are included in the foregoing estimates.



These estimates are based on assumed revenues, previously analyzed, and assumed operating ratios, which, of course, are influenced greatly by operating revenues. Future expenditures for both maintenance and transportation should be affected favorably by the debtor's current rehabilitation program. It should be noted, however, that the estimates, according to the testimony of witnesses [195] for the debtor, are based not only upon the assumption that there will be increases in rates but that there will be no increase in operating costs, either through prices of materials or wages. Furthermore, the estimates of income available for interest on funded debt omit deductions of any amount for the creation and maintenance of the various funds proposed under the debtor's plan.

Although the net income available for interest of the debtor for the year 1936 exceeded its estimate for 1936, the debtor's estimates of net income available for interest for the future, when considered in the light of its past earning experience, appear unduly optimistic. It is reasonably certain that some traffic diverted in recent years to motor carriers will not be regained. Strenuous competition must be expected not only from those carriers but from water carriers and, especially, from other strong railroads serving the same territory as the debtor. This latter competition compels the movement of trains on schedule regardless of the load. Long stretches of the territory through which the debtor's road extends is sparsely populated and productive of little

or no traffic. The debtor's volume of traffic is subject to wide fluctuations, and the topography of the country entails expensive helper service over sharp summits. These factors have and necessarily will have considerable effect on the debtor's income.

#### Value for Rate-making Purposes

Under section 19a of the Interstate Commerce Act, the Commission, by division 1, in *Western Pacific Ry. Co.*, 29 Val. Rep. 239, reported the value for rate-making purposes of the property owned by the debtor to be \$63,321,000 as of June 30, 1914. In similar proceedings, the Commission, by division 1, reported the value for rate-making purposes of the properties of the debtor's wholly owned [196] subsidiaries, Sacramento Northern Railway, Tidewater Southern Railway Company and Deep Creek Railroad Company in the total amount of \$18,336,529 as of their respective valuation dates. If there be added to the above amounts capital expenditures between valuation dates and December 31, 1935, the total would be \$144,619,851.

#### Classes of Creditors and Stockholders

Pursuant to the provisions of the Bankruptcy Act, the district court entered an order, on August 20, 1935, dividing creditors and stockholders for the purposes of the plan and its acceptance, into the following classes: Class 1, first mortgage bonds; Class 2, general and refunding bonds; Class 3, debtor's secured promissory notes to A. C. James Co.; Class 4, debtor's secured promissory notes to Reconstruction Finance Corporation; Class 5, debtor's

secured promissory notes to the Railroad Credit Corporation; Class 6, equipment obligations to Baldwin Locomotive Works (assigned to Fidelity-Philadelphia Trust Co., trustees); Class 7, equipment trust certificates under agreement March 1, 1923; Class 8, equipment trust certificates under agreement dated March 15, 1924; Class 9, equipment trust certificates under agreement dated May 1, 1929; Class 10, debtor's obligations as to advances made on open account by the Western Pacific Railroad Corporation; Class 11, debtor's obligations as to advances made on open account by The Western Realty Company; Class 12, debtor's preferred stock; Class 13, debtor's common stock; Class 14, all other claims, obligations and liabilities not hereinbefore specifically described.

As of December 31, 1936, Class 1 items consisted of \$49,290,100 principal amount of first mortgage 5 percent bonds, on which unpaid interest amounted to \$8,214,766; Class 2 items consisted of \$18,999,500 principal amount of general and refunding mortgage 5 percent bonds, entirely pledged as collateral for certain of the [197] debtor's notes; Class 3 items consisted of \$4,999,800 face amount of notes to A. C. James Company, on which unpaid interest amounted to \$749,970, and which are secured by \$4,249,500 principal amount of debtor's general and refunding bonds, and a second lien upon \$2,000,000 principal amount of the same issue of bonds held by the Railroad Credit Corporation; Class 4 items consisted of \$2,963,000 face amount of notes

to the Reconstruction Finance Corporation, on which that corporation claims unpaid interest of \$544,310, the notes being secured by \$10,750,000 principal amount of debtor's general and refunding bonds, and voting trust certificates for half of the voting stock of The Denver and Rio Grande Western Railroad Company, and a second lien upon \$2,000,000 principal amount of the same issue of bonds held by the Railroad Credit Corporation; Class 5 items consisted of \$2,482,218 face amount of notes to the Railroad Credit Corporation, on which that corporation claims unpaid interest of \$114,156; which notes are secured by \$4,000,000 principal amount of debtor's general and refunding bonds, and a second lien upon the security held by the Reconstruction Finance Corporation; and an assignment of certain advances by The Western Pacific Railroad Corporation, and an assignment of the distributive share of the debtor under the Marshalling and Distributing Plan, 1931; Class 6, 7, 8 and 9 items consisted of various equipment obligations aggregating \$2,048,190; Class 10 items consisted of \$5,757,650 principal amount of advances to the debtor by The Western Pacific Railroad Corporation, on which unpaid interest amounted to \$1,430,957; Class 11 item consisted of \$50,000 principal amount of advances to the debtor by the Western Realty Company, on which unpaid interest amounted to \$6,667; Class 12 items consisted of \$28,300,000 par value of the debtor's preferred stock; Class 13 items consisted of [198] \$47,500,000 par value of

the debtor's common stock; and Class 14 items consisted of various other claims not specifically described by the court.

### Proposed Plans of Reorganization.

The capital structures proposed for the reorganized company in the three plans filed and which would result if modified in accordance with suggestions of the debtor during the hearing and on brief, the distribution of the new securities to be issued under the plans, and the main features thereof, are summarized below.

Existing equipment obligations would not be disturbed under any of the plans. As filed, the debtor's plan would become effective as of January 1, 1936. The debtor later suggested January 1, 1937, as the effective date the same as in the other plans.

The plan of reorganization originally submitted by the debtor contemplated the initial issue of \$25,675,900 principal amount of new first mortgage 4 percent bonds, \$41,774,796 principal amount of new 5½ percent income mortgage bonds (cumulative for the income period in which such interest is payable and for the 4 income periods next succeeding the income period in respect of which such interest is payable), of which \$20,887,398 would be series A bonds, and \$20,887,398 would be series B bonds, \$8,092,709 principal amount of new non-cumulative junior lien 6 percent income bonds, or a total of \$75,543,405 principal amount of bonds. The plan further provides that 926,622 shares of new no-



par common stock be authorized, of which 300,000 shares would be issued forthwith, and 626,622 shares would be reserved for issue upon conversion of \$20,887,398 of the new income bonds.

Under the debtor's plan, its existing first mortgage 5 percent bonds would be exchanged for 30 percent of the new first mortgage 4 percent bonds, and 70 percent of new income mortgage 5½ percent [199] bonds plus additional income bonds equal in face amount to the unpaid interest. Ten million dollars of the new first mortgage 4 percent bonds would be sold at par to the Reconstruction Finance Corporation to provide new money for the reorganized company. In consideration of that purchase, the Reconstruction Finance Corporation would be given for its claim against the debtor treatment equivalent to that given to the holders of the existing first mortgage bonds.

The new junior lien income 4 percent bonds would be issued to the Railroad Credit Corporation and A. C. James Company in settlement of their claims, each to receive new bonds equal in face amount to the principal of their claims plus unpaid interest.

All the new stock would be placed in a voting trust under which 3 voting trustees nominated by the debtor and approved by the bondholders' committee would act pursuant to a voting trust agreement which would be acceptable to the debtor and the bondholders' committee. The voting trust would continue until 10 years from the date of confirma-

tion of the plan. A majority of the debtor's board of directors would be nominees of the holders of income bonds, and as long as the Reconstruction Finance Corporation holds more than \$500,000 of the first mortgage bonds, the voting trustees would elect to the board of directors a person designated or nominated by that corporation. In respect of the 300,000 shares of common stock immediately issuable under the plan and of the shares which may be issued on conversion of the income bonds, voting trust certificates would be issued. The certificates for 150,000 shares of the common stock would be placed in escrow with the trustee of the income mortgage and would be given to the holders of income mortgage bonds if, commencing April 1, 1941, full interest was not paid on the income bonds in respect of the next preceding income period for any [200] deficiency in payment of full interest at the price of \$27.50 per share.

The debtor's plan further provided that there be created a contingency reserve fund of \$500,000 to be available for the purpose of paying fixed interest charges, principal on and dividends on equipment obligations and operating expenses which could not otherwise be provided for without, in the opinion of the board of directors, unduly impairing free working capital. The fund would be created initially from the proceeds of the \$10,000,000 of new first mortgage bonds to be sold in the reorganization, and thereafter maintained out of the net income remaining after the payment of fixed charges.

There would be created also out of available net income before the payment of interest on income bonds a capital fund to be applied for capital investments made in the calendar year in which the fund is set aside, and no additional securities would be issued against such expenditures. The amount set aside in the capital fund for any calendar year would not exceed \$500,000 during the years 1936 to 1940, inclusive, \$1,000,000 during the years 1941 to 1945, inclusive, and in all subsequent years not more than 3 percent of gross revenues.

Provision for a sinking fund in an amount not exceeding in any calendar year one-half of 1 percent of the principal amount of the new income bonds, Series A, also is made in the plan. The fund would be created and maintained out of net income remaining after payment of fixed charges, maintenance of the reserve fund, capital fund, and interest payments on income bonds, and would be applied to the redemption of the series A income bonds.

The debtor's plan also provides for an additional interest fund to be created and maintained out of net income remaining after [201] payment of fixed charges, payments in respect of the reserve fund and the capital fund, interest on income mortgage bonds and junior lien bonds. The fund would not exceed one year's interest on all outstanding first mortgage bonds and would be available only for the payment of interest on such bonds.

During the hearing and on brief, counsel for the debtor suggested that the debtor's plan be modified by providing that, (1) the rate of interest on all bonds be 4 percent per annum, (2) there be created sinking funds of not less than  $\frac{1}{2}$  percent or more than 1 percent for the redemption of all bonds, (3) the escrow agreement in respect of the 150,000 shares of common stock be modified so that there would not be a peremptory forfeiture on the due date of interest, because such interest may be paid in cash out of the available net income of the next four income periods, and be further modified so that there would be no forfeiture at all if the failure to earn interest was caused by excessive maintenance or undue capital expenditures, (4) the voting trust be eliminated from the plan, and (5) there be issued \$7,245,274 par value of 4 percent noncumulative preferred stock to the Western Pacific Railroad Corporation and the Western Realty Company.

With the effective date of the plan as of January 1, 1937, and modified as suggested, the plan would provide for the initial issue of \$25,675,900 principal amount of new first mortgage 4 percent bonds, \$45,219,530 principal amount of new income mortgage 4 percent bonds, \$8,386,040 principal amount of new junior lien income 4 percent bonds, or a total of \$79,281,470 principal amount of bonds, \$7,245,274 par value of new 4 percent preferred stock, and 300,000 shares of no par common stock.

Under the bondholders' plan, the reorganized company would issue initially \$19,858,020, principal amount, of new first mortgage [202] 4 percent bonds, \$19,716,040 principal amount of new income mortgage 5 percent bonds (cumulative against only 3 years income); or a total of \$39,574,060 principal amount of new bonds. The plan further proposes the issue of \$27,930,800 par value of new participating 6 percent preferred stock (cumulative only to the extent that dividends are earned), and not less than 339,995 shares nor more than 489,995 shares of new no par common stock.

The existing first mortgage 5 percent bonds would be exchanged 20 percent for new first mortgage 4 percent bonds, 40 percent for new income mortgage 5 percent bonds, and 40 percent for new participating 6 percent preferred stock, accrued interest also being commuted into the latter stock. As provided in the debtor's plan, \$10,000,000 of the new first mortgage 4 percent bonds would be sold to provide new money for the reorganized company.

The claims of the Reconstruction Finance Corporation, Railroad Credit Corporation and A. C. James Company would be converted into the new common stock (taken at \$100 per share) on the basis of the collateral pledged under the debtor's notes to those creditors. Such stock, amounting to 189,995 shares, would be deposited under an escrow agreement subjecting the stock to purchase warrants.



The Western Pacific Railroad Corporation would be allotted, purchase warrants, entitling the holders thereof to purchase on or before December 1, 1941, all or any part of the 189,995 shares of the new common stock at the price of \$62 per share, plus interest thereon at the rate of 4 percent per annum from January 1, 1937. In addition to its option under the escrow agreement the Western Pacific Railroad Corporation would be granted, through issue to it of subscription warrants, the first opportunity to provide the \$10,000,000 of required new money, receiving therefor the \$10,000,000 [203] new first mortgage 4 percent bonds and 150,000 shares of the new common stock.

To the extent that the Western Pacific Railroad Corporation should fail to exercise the subscription warrants, the bondholder's plan provides that the new money be provided, upon less favorable terms to the debtor by the Reconstruction Finance Corporation, Railroad Credit Corporation and A. C. James Company; and to the extent that they in turn should fail to provide it, the plan provides that it be supplied upon still less favorable terms by the present first mortgage bondholders.

The bondholders' plan further provides that control of a majority of the board of directors of the reorganized company be vested in the new preferred stock until the reorganized company shall have demonstrated its capacity to pay a continuous return on that stock. A contingency reserve fund and a capital fund, similar in all respects to those proposed

by the debtor also are provided for in the bondholders' plan. It also provides for a one-half percent sinking fund for the redemption of the new income bonds, but only after payment of fixed and other contingent charges and the payment of dividends on preferred stock.

The plan submitted by the A. C. James Company proposes that the reorganized company issue initially \$10,000,000 principal amount of new first mortgage 4 percent bonds, \$49,290,100 principal amount of new general mortgage 4 percent income bonds (cumulative only to the extent that interest is earned), and \$10,450,263 principal amount of new noncumulative 4 percent debentures (convertible into 150 percent of their principal amount in 6 percent preferred stock), or a total of \$69,740,363 principal amount of new bonds and debentures. The preferred stock of the debtor, of which \$28,300,000 par value is now outstanding, would be delivered to the debtor under this plan [204] and \$5,807,650 par value of such stock would be reissued. The common stock of the debtor, now outstanding of the par value of \$47,500,000, would be delivered to the debtor and be reissued.

The existing first mortgage 5 percent bonds would be exchanged for the new general mortgage 4 percent income bonds, with a bonus of \$500 par value of common stock for each \$1,000 bond. The new noncumulative 4 percent debentures would be allotted to the Reconstruction Finance Corporation, Railroad Credit Corporation and A. C. James Com-

pany, and those creditors would be given also a bonus of \$500 par value of common stock for each \$1,000 of the debtor's notes owned by them. The \$5,807,650 par value of preferred stock would be issued to the Western Pacific Railroad Corporation and the Western Realty Company in settlement of the principal amount of their claims against the debtor.

~~Under this plan~~ all accrued interest upon all outstanding debt would be canceled.

The \$10,000,000, principal amount, of new first mortgage bonds would be sold to provide new money for the reorganized company and the Western Railroad Corporation would be given the right first to purchase such bonds, with a bonus at the rate of 15 shares of the common stock for each \$1,000 first mortgage bond purchased.

No reserve capital or sinking funds are provided for under the James plan.

Each of the three plans sets forth in more or less detail the proposed manner of participation of the stockholders and creditors in the plan and the method of consummation. The debtor's plan provides that it shall not be declared operative or carried out until finally approved by the Commission and confirmed by the court after acceptance by the holders of each class or classes of securities or claims affected by the plan as shall be sufficient under the [205] provisions of the Bankruptcy Act. The James plan provides that it shall not be carried out until it shall have been approved by the

Commission and the court, pursuant to the requirements of the Bankruptcy Act, and until it shall have been accepted by two-thirds of the creditors of each class, and by two-thirds of the stock of each class. The bondholders' committee plan provides that the plan shall not be carried out until it shall have been accepted by the holders of at least two-thirds in principal amount of the debtor's outstanding first mortgage bonds, nor unless either (1) the plan shall have been accepted by creditors holding at least two-thirds in principal amount of the total allowed claims of such class, and by the holders of at least two-thirds of the stock of each class, or (2) provision shall have been made for the sale of the debtor's property at public auction at a fair upset price as determined by the court, and the payment to the non-assenting creditors of such class or the non-assenting stockholders of such class, of their aliquot portion of the proceeds of the sale of such property.

None of the proposed plans is agreed to by all the parties to the proceeding.

The debtor's plan is objected to by the bondholders' committee on the grounds that it proposes an unsound capital structure in that the ratio of debt to capital stock is disproportionate, and that the total of fixed and contingent interest charges proposed is excessive in the light of the debtor's past earning experience and probable future earnings. The James plan is objected to for the same reasons. The bondholders further contend that the debtor's

plan discriminates unfairly in favor of the Reconstruction Finance Corporation and against the first mortgage bondholders and the Railroad Credit Corporation in that it proposes to place the Reconstruction Finance Corporation on a parity with the present first mortgage [206] bondholders as compensation for furnishing the \$10,000,000 of new money by the Finance Corporation. In proposing to give the A. C. James Company and the Railroad Credit Corporation securities on the basis of the principal amount of their notes, irrespective of the amount of their collateral security, the bondholders allege that the Railroad Credit Corporation is discriminated against. By granting all the new common stock of the reorganized company to the Western Pacific Railroad Corporation without requiring any contribution or sacrifice by that corporation to or in the reorganization, the bondholders allege that undue preference is proposed.

The James plan is further protested by the bondholders' committee on the grounds that it is discriminatory in that it does not provide any fixed interest obligations for the present first mortgage bonds; it proposes the issue of new securities having the sole first lien upon the property of the reorganized company exclusively to the Western Pacific Railroad Corporation along with a bonus of \$150 par value of new common stock for each \$100 bond; proposes the waiving of all accrued interest without any compensation therefor; disregards the relative priorities of the various creditors by giv-



ing the same bonus of new common stock; proposes no sinking funds for retirement of debt; makes the new bonds proposed to be given the present first mortgage bondholders mature in 1987 as against a maturity in 1977 for the obligations which are proposed to be given to the so-called junior creditors; and proposes to treat the claims of the Reconstruction Finance Corporation, the Railroad Credit Corporation and the A. C. James Company on the basis of the principal amounts of the notes rather than upon the basis of the collateral held. The bondholders' committee also objects to the James' plan proposal to give the Reconstruction Finance Corporation, the [207] Railroad Credit Corporation and the A. C. James Company the principal amount of their notes in new 4 percent debentures convertible into 150 percent in principal amount of 6 percent preferred stock. The bondholders' committee points out that if the debentures are converted, the new preferred stock would rank in the scale of distribution of the reorganized company's earnings substantially at the same point at which interest would be paid upon the debentures, and that this would result in a 9 percent annual return upon the present claims; and also would operate to depress the value of the common stock of the reorganized company.

The bondholders' plan is objected to by the A. C. James Company on the grounds that it proposes an unsound capital structure in that it does not furnish appropriate vehicles for senior and junior

financing of future capital requirements; proposes an unduly complicated capital structure; does not preserve debt as debt; capitalizes unearned and unpaid interest as a permanent part of the capital structure; proposes for certain of the new securities to be issued excessive interest rates; and proposes excessive fixed charges. Certain of those objections also are advanced by that company to the debtor's plan. It further alleges that the bondholders' plan discriminates unfairly against the other creditors and in favor of the bondholders, and does not accord sufficient recognition to the debtor's equity. [208]

#### Conclusions

By the provision of subsection (b) of section 77 of the Bankruptcy Act, as amended, a plan of reorganization shall include provisions modifying or altering the rights of creditors generally, or any class of them, secured or unsecured; either through the issue of new securities of any character or otherwise; shall provide for fixed charges (including fixed interest on funded debt, interest on unfunded debt, amortization of discount on funded debt, and rent for leased railroads) in such an amount that, after due consideration of the probable prospective earnings of the property in the light of its earnings, experience and all other relevant facts, there shall be adequate coverage of such fixed charges by the probable earnings available for the payment thereof; and shall provide adequate means for the execution of the plan. Subsection

(c) of section 77 provides that the judge shall approve the plan certified to the court by the Commission if satisfied, after hearing, and without hearing if no objections are filed, that the plan complies with the provisions of subsection (b), is fair and equitable, affords due recognition to the rights of each class of creditors and stockholders, does not discriminate unfairly in favor of any class of creditors or stockholders, and will conform to the requirements of the law of the land regarding the participation of the various classes of creditors and stockholders; that the approximate amounts to be paid by the debtor, or by any corporation or corporations acquiring the debtor's assets, for expenses and fees incident to the reorganization, have been fully disclosed so far as they can be ascertained at the date of the hearing, are reasonable, are within such maximum limits as are fixed by the Commission, and are within such maximum limits to be subject to the approval of the judge; that the plan provides for the payment of all costs of administration and all other allowances made or to be made by the judge, except that allowances for the actual and reasonable expenses (including reasonable attorney's fees) incurred in connection with the proceedings and plan by parties in [209] interest and by reorganization managers and committees or other representatives of creditors and stockholders, and the actual and reasonable expenses incurred in connection with the proceedings and plan and reasonable compensation for services in connection there-

with by trustees under indentures, depositaries, and such assistants as the Commission with the approval of the judge may especially employ, may be paid in securities provided for in the plan if those entitled thereto will accept such payment. The plan approved by the Commission must meet with these requirements of subsections (b) and (c) and be compatible with the public interest.

It will be observed that in so far as the capitalization of a reorganized company is concerned, section 77 contains no limitations other than that the fixed charges of the company shall be adequately covered by the probable earnings available therefor, and the plan as a whole shall be compatible with the public interest. The public interest is not defined, but it would seem obvious that to be compatible with the public interest, the plan must provide a capital structure for the reorganized company which will give it a reasonable opportunity to function efficiently and continuously as a going concern. This requires that the capitalization should not exceed a conservative valuation of the assets to be taken over by the reorganized company, and that proposed charges are within its probable earning power. It is of primary importance; therefore, to ascertain whether the capital structures proposed in the various plans are properly related to assets and earning power.

The aggregate capitalization, exclusive of non-voting stock, under the debtor's plan, if modified as suggested by its counsel, would amount to \$88,-

574,934, or a reduction of \$65,876,850 under its present debt and capitalization. Treating the proposed no-par value stock at \$100 per share, the aggregate capitalization would amount to \$118,574,934, or a reduction of \$35,876,850. Fixed [210] interest bearing obligations would amount to \$27,724,090, but total fixed and contingent interest bearing obligations would amount to \$81,329,660, or an actual increase of \$2,677,876 over present debt. The ratio of debt to total capitalization would be 68.6 percent. The fixed interest charges would be \$1,113,509 per annum, or a decrease of \$2,264,736 under present fixed charges, but total fixed and contingent charges, excluding charges on the so-called interest fund, would amount to \$4,654,139 per annum, or an increase of \$1,275,894 over present interest charges. With \$289,811 dividends on preferred stock, a total of \$4,943,950 would be required before payment of any dividends on common stock.

It is thus seen that under the debtor's plan existing debt is preserved as debt although a larger amount of interest and other charges are made dependent upon earnings. While such provisions might afford temporary relief, the debtor still would be faced with debt maturities which, if they occurred in a period of low earning power or if the debtor had consistently failed to earn the interest charges on the principal, would be difficult or impossible to refund. A capital structure proposing an increase of \$1,275,894 in charges when for several years past present charges have not been met,



cannot be considered as sound or in the public interest.

The bondholders' plan, exclusive of no-par value stock, contemplates an aggregate capitalization of \$69,553,056, or a reduction of \$84,898,728 under the debt's present debt and capitalization. Treating the proposed no-par value stock at \$100 per share, the aggregate capitalization would be a minimum of \$103,552,556, and a maximum of \$118,552,556, or a reduction of \$50,899,228 or \$35,899,228 respectively under present debt and capitalization. Fixed interest bearing obligations would amount to \$21,906,210, and the total of fixed and contingent interest bearing obligations would [211] be \$41,622,250, or a reduction of \$37,029,534 under present debt. The ratio of debt to total capitalization would be 41 percent or 35 percent. Fixed interest charges would be \$880,793 per annum, or a reduction of \$2,497,452, and total fixed and contingent charges \$3,063,755 or a reduction of \$314,490 below present interest charges. Including dividends of \$1,675,848 on preferred stock, a total of \$4,739,603 would be required before any dividends could be paid on common stock. Total charges of \$4,542,443 would have to be met before any amount could be applied to the proposed sinking fund for income bonds.

Under the James plan, the total capitalization would be \$125,096,203, or a reduction of \$29,355,581 under present debt and capitalization. Fixed interest bearing obligations would amount to \$12,048,190, or a reduction of \$66,603,594, but total fixed

and contingent debt would amount to \$71,788,553, or a reduction of only \$6,863,131 under present debt. The ratio of debt to total capitalization would be 57 percent. While fixed interest charges of only \$486,473, or a reduction of \$2,891,772, are proposed, total fixed and contingent interest would amount to \$2,876,088, exclusive of any provisions for capital sinking funds. It is thus seen that the James plan proposes a debt structure quite similar to that proposed by the debtor.

Considering the past and present earning power of the debtor on the basis of the facts heretofore recited with respect to traffic and earnings, the Commission should find that none of the debt structures, as proposed in the plans before it, should be approved as compatible with sound financing and the public interest.

From a consideration of the data herein set out, it is clear that the effect of adjusting the earnings of the debtor's system available for interest during the period 1931 to 1935, inclusive, to reflect normal maintenance, social security and retirement legislation [212] now in effect, and by elimination of amortization of bond discount included in the accounts, would be to show deficits in earnings available for interest amounting to approximately \$850,000 in 1931 and \$400,000 in 1932, and practically no earnings would be available in 1933, \$500,000 in 1934, and \$250,000 in 1935. But limitation of the fixed charges of the reorganized company on the basis of such hypothetical adjustments can hardly

be justified, since other factors, now unknown, tending to increase net earnings may later affect the situation. Further, limitation of fixed charges in this case on the basis of the minimum of earnings shown to have been available would appear too severe and an average of the available earnings over a period in which the company might be expected to finance its need through short term borrowing seems reasonable. It is observed that after substantial earnings in 1930 and with deficits in earnings available in 1931 and 1932, the debtor earned in 1933 the sum of \$674,007 for fixed charges. And the adjusted earnings would show after substantial earnings in 1930, deficits or no earnings in the next three years, and available earnings of close to \$500,000 in 1934. These data cover the critical period through which the debtor has recently passed, and indicate that fixed charges of \$500,000 could have been paid with reasonable support from the banks. They show equally clearly that no fixed charges in excess of that approximate sum should be carried, since actual earnings were insufficient for three consecutive years, to pay substantially more than \$500,000, and the adjusted earnings would have been insufficient for four years in succession.

With annual interest charges on existing equipment obligations amounting to \$86,473 per annum, it is recommended that the plan approved by the Commission provide for the immediate issue of not to exceed \$10,000,000, principal amount, of new

first mortgage bonds, [213] and that no other fixed interest obligations be permitted. These bonds should be secured by a new first mortgage which should be a first lien upon all property, real and personal, and equipment of the reorganized company now pledged under existing mortgages of the debtor. To facilitate future capital financing, the total authorized issue of bonds thereunder should be limited to \$50,000,000, of which \$10,000,000 should be sold to provide the new money required in the reorganization, and the remainder reserved to be issued to provide for, or to reimburse the reorganized company for expenditures for additions, betterments, improvements or extensions made after the effective date of the reorganization, in a principal amount not exceeding 75 percent of the actual cost of such additions, betterments, improvements or extensions. The bonds should mature in 30 years, bear interest at the rate of 4 percent per annum payable semi-annually, and be redeemable, in whole or in part, on any interest payment date upon 30 days notice, at their principal amount and accrued interest.

Considering the limited amount of fixed interest bonds recommended herein, there would seem to be no real reason for the creation and maintenance of the so-called contingency reserve fund of \$500,000 to be available for the payment of interest on the new first mortgage bonds as proposed in the debtor's and bondholders' plans. It is recommended,

therefore, that no provision be made for such a fund.

Since new first mortgage bonds would not be issued in principal amount to exceed 75 percent of future capital expenditures, the balance of such expenditures must be financed through the issue of junior securities or from earnings. Under both the debtor's plan and the bondholders' plan funds for such expenditures would be secured from the heretofore described capital fund contemplated by their plans. While the A. C. James Company opposes the creation [214] of such a fund, as well as a sinking fund for the redemption of bonds, it does not contend such funds are not in accordance with the principles of sound financing, but that the Revenue Act of 1936 places too great a penalty on the retention of earnings for such purposes. It is essential, however, that the reorganized company should not be embarrassed in securing funds for future capital expenditures. It also is believed to be desirable that provision be made at least for the retirement of the income bonds. It is recommended, therefore, that the plan approved by the Commission provide for the creation of a capital fund out of available net income remaining after payment of fixed interest. To avoid too heavy a sacrifice by present security holders, payments into the fund should not exceed \$500,000 in any one year, nor, in any event, the sum needed to raise the totals of the fund to \$1,000,000 at any time, and payment



into the fund should be dependent upon earnings and non-cumulative.

Available net income should be determined for each period of six months ending June 30 or December 31, (called income periods) beginning with the income period ending June 30, 1937. Available net income for each income period should be determined by deducting from the consolidated income of the reorganized company and its subsidiaries available for fixed charges for such income period, determined in accordance with accounting rules of the Commission, all fixed charges of the reorganized company and its subsidiaries accrued during such income period; provided, however, that in determining available net income there shall not be deducted any amounts expended in connection with the rehabilitation program out of the \$10,000,000 of new money to be provided in the reorganization (or out of the proceeds of any trustees' certificate or other obligations retired out of said money), notwithstanding that under the accounting rules [215] hereinbefore mentioned certain of such expenditure may be chargeable as operating expenses.

With respect to sinking funds, the debtor suggests that such a fund should be provided for all bonds, while the bondholders propose that it apply to income bonds only. The debtor also proposes that such a fund should be created and maintained out of available net income remaining after payment of interest and provision for the capital fund, while the bondholders propose that payments into

the fund should not be made until after payment of dividends on preferred stock. The latter provision, however, would not only delay but possibly preclude the retirement of such bonds. On the other hand with such a limited amount of fixed interest bonds as recommended herein, it would not seem essential to provide for their retirements through a sinking fund. It is recommended, therefore, that provision should be made in the plan approved by the Commission for the creation and maintenance of a sinking fund of one-half of 1 per cent to be used for the retirement of income bonds hereafter recommended out of available net income remaining after the payment of fixed charges, payment into the capital fund, and interest on income bonds.

In order that the contingent interest bonds issued in the reorganization should be a saleable security easily refundable at maturity, their interest charges should be well within the apparent earning power of the company under reasonably favorable business conditions. The marked increase in the net earnings of the debtor in 1936 over 1935 indicates a substantial recovery of traffic. Forecasts of higher earnings in 1937 may be supported by the record, but at this time the period during which such higher earnings may continue is problematical. It appears that the period of marked low earning power of the debtor embraces the years 1931 to 1935, inclusive. The total of the fixed and

contingent interest charges plus sinking [216] fund requirements and the capital fund of the reorganized company should be not more than the earnings of the debtor available for interest in 1936. The last year prior to 1936 in which the debtor's earnings were sufficient to pay such charges was 1929.

If the above recommendations are approved, charges on equipment obligations, new first mortgage bonds and proposed capital fund, would require \$986,473 per annum. Since the amount available for interest in 1936, the most recent full calendar year, after eliminating the extraordinary expenditures for rehabilitation, amounted to \$1,766,632, it is recommended that the new income bonds to be issued should not exceed \$19,716,040 in principal amount, and should bear interest at the rate of 4 percent per annum. Interest on such bonds would amount to \$788,642, and including charges for the sinking fund, the total of the fixed and contingent charges recommended would amount to \$1,873,695.

The new income bonds should be secured by a mortgage, such mortgage to constitute a lien, subject only to the lien of the first mortgage, upon all property from time to time subject to the lien of the first mortgage. The total authorized issue of bonds thereunder should be limited to \$19,716,040. The bonds should be dated as of the effective date of the reorganization and should mature in 50 years, bearing interest payable semi-annually only out of the available net income, such interest to be cumu-

lative only as against such available net income for the income period in respect of which such interest is payable. The bonds should be redeemable on any interest payment date at their principal amount plus any interest payable thereon on such interest payment date. The available net income out of which such interest is payable should be that remaining after the payment of fixed charges and such amounts [217] as may be required to maintain the capital fund. Such bonds also should be entitled to the benefit of a one-half of 1 percent cumulative sinking fund, payable out of available net income remaining after the payment of all prior charges heretofore recommended.

The debtor's assets consisting of real and personal property have been described, and its investment in such property has been stated. While these data alone would seem to support the total capitalization proposed in each of the three plans, yet when considered in connection with its record of earnings, it appears that the total capitalization of the reorganized company should be less than that proposed in any of the plans if any material return in the future on the reorganized company's capital stock is to be expected.

The maximum of earnings available for interest forecast by the debtor is approximately \$4,000,000 for 1940, based on assumed revenues of \$21,632,200, 7.5 percent in excess of the maximum of the debtor's revenues in any year since 1922. Prior charges heretofore provided for amount to \$1,873,695 which

deducted from \$4,000,000 leaves \$2,126,305 of possible additional annual earnings under the debtor's estimate, to be capitalized, if there is to be a reasonable prospect of a return on the securities to be issued. This sum would pay preferred stock dividends of 5 percent and common stock dividends of 3 percent on slightly less than \$60,000,000 par value of stock divided equally between preferred and common. The Commission should approve the issue under the plan of 295,740  $\frac{3}{5}$  shares of preferred stock, \$100 par value, and 300,682  $\frac{1}{5}$  shares of \$100 par value common stock, and in view of the data of record relating to past earnings and the forecasts of future earnings, should find that such issue, together with the securities hereinbefore approved, constitute the maximum amount of capitalization which may be issued under the plan. [218].

The new preferred stock, which should be authorized in the total amount of 500,000 shares, should be entitled to receive dividends at the rate of 5 percent per annum in respect of each calendar year before any dividends be paid or declared upon the common stock. Such dividends should be cumulative to the extent earned in respect of any calendar year but not paid; but such dividends should otherwise be noncumulative. After dividends shall have been paid or declared on any new common stock at the rate of \$3 per share in respect of any year, each share of new preferred stock should be entitled to share equally with each share of any new common stock in any dividends paid or declared in re-



spect of such year. In event of liquidation the new preferred stock should be entitled to receive out of the assets of the reorganized company its par value before any distribution is made to any new common stock but should not be entitled to any further participation in such assets. The new preferred stock should be redeemable, in whole or in part, at any time at its par value plus accrued and unpaid cumulative dividends.

The plan should provide further that the reorganized company should not, without the vote or consent of the holders of at least two-thirds in par value outstanding new preferred stock (1) create or permit to be created any mortgage or other lien upon any of its properties, excepting the new first mortgage and new income mortgage or purchase money liens (including equipment obligations) upon property hereafter acquired, given for not more than 75 percent of the purchase price of such property; (2) create or issue any bonds, notes or other evidences of indebtedness maturing more than 2 years from their date, except purchase money obligations [219] given for not more than 75 percent of the purchase price of property hereafter acquired; (3) create any stock ranking, either as to assets or dividends, in priority to or on a parity with, the new preferred stock, or (4), permit any subsidiary, all of whose stock, except directors' shares, shall be owned by the reorganized company, to create any mortgage or other lien upon any of its properties or issue any such bonds, notes or

other evidences of indebtedness (except purchase money liens or obligations as aforesaid), or issue any additional stock of any class, unless the obligations secured by such mortgage or other lien or such other obligations or such stock shall be acquired by the reorganized company. Each share of the new preferred stock should have equal voting rights and privileges with any new common stock.

The total authorization of the common stock should be 500,000 shares. Including the above charges, an amount of \$4,254,445 would be required before the reorganized debtor could pay a 3 percent dividend on an issue of \$30,068,220 par value of common stock.

Under the above recommendations, the total capitalization would be \$91,406,510, consisting of \$2,048,190 equipment obligations, \$10,000,000 first mortgage 4 percent bonds, \$19,716,040 non-cumulative income mortgage 4 percent bonds, \$29,574,060 noncumulative 5 percent preferred stock, and \$30,068,220 common stock. Total fixed interest charges would be \$486,473, total fixed and contingent charges including capital and sinking funds, would be \$1,873,695, total preferred dividends would be \$1,478,703 or a grand total of \$3,352,398.

The allocation of the new securities of the reorganized company must comply with the provisions of subsection (e) of section 77, hereinbefore stated. The language comprising those provisions has long had a settled meaning in equity reorganizations.

[226] Briefly stated it is to the effect that no plan of reorganization will be fair and equitable if it attempts to secure the rights and interests of stockholders at the expense of the prior rights of secured or unsecured creditors. Subsection (e) specifically commands that the rights of each class of creditors and stockholders be accorded due consideration.

All three plans before the Commission are predicated on the priority of the first mortgage over the general mortgage, and all parties admit that the first mortgage is a first lien on the main line of the debtors' railroad and the securities physically pledged under that mortgage. The trustee under the first mortgage and the holders of bonds secured by that mortgage contend that the first mortgage is a first lien on substantially all the debtor's property, except equipment subject to existing leases, conditional sale agreements or equipment trust agreements. The general mortgage trustee and those creditors with whom are pledged general mortgage bonds contend, however, that the first mortgage is not a lien, or is a lien only to the extent of the proceeds of first mortgage bonds expended thereon, on cash and collateral held by the trustees under the general mortgage, or the Northern California extension, on the debtor's equity in rolling stock subject to leases, conditional sale agreements or equipment trust agreements, and on property, in general, purchased either in whole or in part from free funds. Those parties contend further

that most of the property just described is not only free from the lien of the first mortgage but is subject to the lien of the general mortgage, and that its value is sufficient for the full payment of all the debts secured under the general mortgage, with interest. With the exception of the A. C. James Company, they assert that the first mortgage bondholders are not entitled to preferential treatment.

[221]

While final adjudication of this and similar questions must be made by the court, in the absence of such adjudications, it becomes the duty of the Commission to preliminarily determine them for the purposes of consideration of any of the plans before it. Since most of the property which is in dispute was acquired after the date of the first mortgage, the primary question involved is whether such property is covered by the after-acquired property clause contained in the granting clauses of the first mortgage.

Clause First of the granting clauses covers both in detail and by a general statement all property which had been owned by the debtor's predecessor, except only cash items.

Granting Clause Third covers "any and all property and facilities of any and every kind and description \* \* \* which may from time to time hereafter be acquired or constructed by or belong to" the debtor if such after-acquired property falls within one of four specified categories:

(1) If any "First Mortgage Bonds or proceeds thereof or cash deposited" under the first mortgage have been authenticated or paid out "on account of the purchase, acquisition or construction thereof or work therein;" or

(2) If the property constitutes "an integral part or parts of lines of railroad, extensions, branches or other property subject to the lien" of the first mortgage; or

(3) If the property is "used or acquired for use in or for the maintenance or operation of or pertaining to" any of the property subject to the lien of the first mortgage; or

(4) If the property consists of shares of stock or of other securities of the Salt Lake City Union Depot and Railroad Company or Standard Realty and Development Company or any subsidiary as defined. [222]

Granting Clause Fifth covers almost every kind of property and facility used or useful in the operation of a railroad (including additional tracks, spurs, equipment, material and supplies, land) ending with the generality "all other property of every description and all rights and interests in or with respect to the use of property \* \* \* whether now owned \* \* \* or at any time hereafter acquired," if "appurtenant to or used or held for use as, or as a part of or as parts of, or to facilitate or safe-



guard the maintenance or operation of, any lines of railroad, extensions, branches \* \* \* or other properties now or at any time hereafter subject to the lien" of the first mortgage.

Following granting Clause Sixth is a proviso permitting the debtor by the use of free funds to acquire property free of the lien of the first mortgage if such property is not of the character described in the four subdivisions of granting Clause Third.

The Northern California extension, various branches and spurs, and equipment used under leases, or contracts or equipment trust agreements are the principal items of property in dispute. With respect to the first two classes of property we are satisfied from the record that substantial amounts of the proceeds of first mortgage bonds were used in their acquisition or construction or at least "on account of the purchase, acquisition or construction thereof or work thereon." We construe the latter language to mean that the lien of the first mortgage attaches to after acquired extensions if the purchase, acquisition or construction thereof, or any work thereon, be financed in any part with first mortgage bonds or cash deposited under that mortgage.

While the construction of the Northern California extension was financed in part with the proceeds of certain debentures which were subsequently exchanged for general and refunding bonds, it is [223] not contended that the debentures were secured by

a lien on the extension. Moreover the record is clear that there was no intent to create a purchase money lien on the extension in favor of the debentures. The same is true with respect to the advances from the Reconstruction Finance Corporation; and the general and refunding mortgage was not executed and delivered until several months after the completion of the extension.

The Commission should conclude, that, in determining the equitability of plans of reorganization for the debtor, the lien of the general mortgage on the Northern California extension and various branches and spurs in question should be considered subject to the lien of the first mortgage.

The debtor's equity in rolling stock subject to leases, conditional sale agreements or equipment trust agreements, would seem to be covered by the after-acquired property clause in the third paragraph, as well as by the fifth paragraph, of the granting clauses unless the proviso at the end of the granting clauses negatives such a construction. The proviso reads as follows:

\* \* \* ; and the company may, unless First Mortgage Bonds shall have been authenticated and delivered or their proceeds or other cash deposited hereunder paid out against the same, purchase and acquire equipment free from the lien hereof, by lease, conditional sale agreement or under any form of equipment trust, or purchase such equipment and issue obligations therefor

secured by mortgage or pledge of such equipment superior to the lien of this indenture.

The latter provision, however, should be construed both in the light of the language which precedes it in the same paragraph [224] and in the light of the paragraph which follows the habendum clause. The latter paragraph reads as follows:

"Subject, however, as to all equipment now owned to the equipment trust or conditional sale agreements secured thereon, to the equipment trust or conditional sale agreements to which the same shall be subject as permitted hereby \* \* \*"

If all equipment acquired under equipment trusts was to be entirely free of the lien of the first mortgage, it is not understood why the words "equipment trust or conditional sale agreements to which the same shall be subject as permitted hereby" were made part of the last quoted provision. The Commission should consider, for the purposes of a plan of reorganization, that since the equipment in question was acquired for use, and was actually used, on the mortgage lines, the debtor's equity in that equipment is subject to the lien of the first mortgage.

The Commission also should consider that the property characterized as non-carrier real estate which was owned by the predecessor of the debtor and which the general and refunding mortgage trustee contends did not become subject to the lien

of the first mortgage because the reorganization plan, pursuant to which the present first mortgage bonds were issued, contemplated that they should have a lien ~~only~~ upon railway properties, is covered by the first mortgage. No such distinction as urged by the general mortgage trustee, appears in the language of the mortgage itself, and it is not clear that the use of the words "railway properties" in the plan of reorganization was intended to exclude property which was classified as non-carrier for valuation purposes by the Commission many years thereafter. [225]

With the exception of the notes of the Deep Creek Railroad Company and the Standard Realty & Development Company, there is no contention that the cash and collateral held by the trustee under the general and refunding mortgage are not free from the lien of the first mortgage. While due recognition must be accorded to the rights of the creditors with whom are pledged general mortgage bonds, those creditors are not entitled to the same treatment as first mortgage bond holders; who should be considered as having a first lien upon practically all of the assets of the debtor. It follows that holders of the debtor's first mortgage bonds should receive securities of a higher rank than other creditors, at least to the extent that existing conditions will permit.

Proceeding to the allocation of the new securities, it has been seen that it is imperative that \$10,-

000,000 of new money be raised for the purpose of retiring trustees' certificates and completing the rehabilitation program. Provision should be made in the plan for the immediate sale of the \$10,000,000 principal amount of the new first mortgage 4 percent bonds hereinbefore recommended. To facilitate the sale of the bonds at par, it is recommended that the plan provide that 10 shares of the new common stock be given to the purchaser of each \$1,000 principal amount of the new bonds.

Existing first mortgage bonds are outstanding in the principal amount of \$49,290,100. Unpaid interest thereon as of January 1, 1937, amounted to \$8,214,766. In this connection the A. C. James Company proposes that all unpaid interest should be waived. It is not contended by that company that such interest is not equally secured with the principal but it is urged that it is improper in a proceeding, such as this to capitalize unearned and unpaid interest. But the Commission should base the capitalization of the [226] reorganized company upon a consideration of assets and earning power rather than on the amount of existing claims, leaving the matter of unpaid interest for consideration in determining the relative rights of the creditors. Circumstances may be such as to render inequitable the allotment of securities to cover unpaid interest but the rights represented by unpaid interest should be recognized with the principal of the debt.



It is recommended, in view of the priority of the existing first mortgage bonds, that all of the new income bonds, \$19,716,040 principal amount, all of the new preferred stock, \$29,574,060 par value, and \$8,214,766 par value of the new common stock hereinbefore recommended be allotted to the holders of existing first mortgage bonds. On this basis the holders of first mortgage bonds would receive 40 percent of the principal of their debt in income bonds, 60 percent in preferred stock, and the unpaid interest thereon in common stock.

Of the total of new securities hereinbefore recommended there thus remains only \$11,853,454 par value of common stock for allocation among the debtor's other creditors and stockholders. That equals the total of the claims of the Reconstruction Finance Corporation, Railroad Credit Corporation, and A. C. James Company. Since their claims are secured by \$18,999,500 principal amount of general mortgage bonds pledged by the debtor, they are clearly entitled to priority over the unsecured claims of the Western Pacific Railroad Corporation and over the claim of the Western Realty Company, a subsidiary of the Western Pacific Railroad Corporation, the latter being also the owner of all of the debtor's capital stock. Obviously, if due recognition is to be given the rights of these secured creditors, the entire amount [227] of common stock remaining for distribution should be allotted to them.

While, as stated, the par value of the stock available for distribution equals the principal and unpaid interest on the secured creditors' notes, the collateral pledged by the debtor as security for the notes is of varying amounts. For instance, the total of the Reconstruction Finance Corporation's claim is \$3,507,310 although it holds as pledgee 56.6 percent of the debtor's general mortgage bonds. The total claim of the Railroad Credit Corporation amounts to \$2,596,374 and 21.1 percent of the general mortgage bonds are pledged thereunder. The total of the A. C. James Company's claim amounts to \$5,749,770 and only 22.3 percent of the general mortgage bonds are pledged thereunder. Under these circumstances it is recommended that the allotment of the common stock to these secured creditors be made on the basis of the collateral held rather than on the amount of the claims. Such allotment would result in the Reconstruction Finance Corporation receiving \$6,709,055 par value, the Railroad Credit Corporation \$2,501,079 par value, and the A. C. James Company \$2,643,320 par value of new common stock.

Since all of the securities that the reorganized company would be justified in issuing are required for the adjustment of the claims of secured creditors and the securing of necessary new capital, the only provision by which the Western Pacific Railroad Corporation, as an unsecured claimant and owner of the debtor's outstanding capital stock,

may properly participate in the reorganization, is by the issue to it of rights to subscribe to the new first mortgage bonds to be sold by the reorganized company. It is recommended therefore that there be issued to that corporation subscription warrants entitling it to purchase at par within, but not [228] later than sixty days after the effective date of the reorganization, all or any part of the \$10,000,000 principal amount of new first mortgage bonds. The Commission should find that the equity of the preferred and common stockholders of the debtor has no value. The claim of the Western Realty Company should be canceled.

The plan should provide further that opportunity to provide such part of the new money as is not provided by the exercise of the subscription warrants allotted to the Western Pacific Railroad Corporation be offered to the Reconstruction Finance Corporation, the Railroad Credit Corporation and A. C. James Company in proportion to the general mortgage bonds now held by them, upon the same terms as offered to the Western Pacific Railroad Corporation. If any of those secured creditors should fail to subscribe for its full proportion, the other or others of such creditors should be permitted to subscribe for the unsubscribed balance, in the proportion which the existing general mortgage bonds held by them respectively bear to the total amount of general mortgage bonds held by the corporations so electing to subscribe for their

full proportion. The contingent rights of subscription granted to those secured creditors should be evidenced by appropriate warrants, and such rights should, in the case of each offering, run concurrently with the rights evidenced by the warrants to be issued to, or on the order of, the Western Pacific Railroad Corporation. Holders of such warrants should be required to elect prior to the expiration of such warrants, in each case, the extent to which they will exercise their subscription rights. Should the Western Pacific Railroad Corporation, or the Reconstruction Finance Corporation, Railroad Credit Corporation, and A. C. James Company fail to provide the new money in accordance with the above terms, holders of first mortgage bonds should be entitled to provide the same upon the same terms and conditions as those parties, and [229] warrants evidencing such rights should be granted to such bondholders.

If the new securities are allocated as recommended above, it would result in preserving the priority of the first mortgage bondholders as to the principal amount of their bonds over all other existing creditors and stockholders in so far as new securities are available. The holders would receive securities bearing a rate of interest 1 percent lower for 40 percent of the principal of their bonds, and the payment of interest and dividends would be contingent on earnings. On the other hand, present stockholders, both preferred and common, as such,

would receive nothing, and the stock allocated to other secured creditors would be subordinate to the securities received by the first mortgage bondholders for the principal of their bonds. The provision for the participation of the unsecured creditor would not discriminate against either the first mortgage bondholders or the other secured creditors because such unsecured creditor must contribute \$1,000 in cash for each new \$1,000 bond and 10 shares of new common stock received.

Under both the debtor's plan and the bondholders' committee plan current liabilities of the debtor incurred in the ordinary conduct of its business prior to the institution of this proceeding, current liabilities and obligations of the debtor and of its trustees incurred during this proceeding, and all other claims, liabilities or obligations for which specific provision is not made in those plans are not to be affected by the plans, but to the extent that such claims, liabilities, or obligations are not paid by the debtor or its trustees pursuant to order of the court, they are to be paid in cash or assumed by the reorganized company. According to the record current liabilities incurred in the ordinary conduct of the debtor's business prior to this proceeding were of a nominal amount. The Commission should approve such provisions. [230]

Each of the three plans before the Commission propose different conditions under which a plan shall be consummated. The James plan affirma-



tively provides that its plan shall not be consummated until accepted by two-thirds of each class of creditors and two-thirds in amount of each class of stock. Reorganizations under section 77 are primarily premised upon the acceptance of plans by two-thirds or more of each class of creditors and stockholders. Congress recognized, however, that the public interest might, under certain circumstances, require the confirmation of a plan of reorganization even though it was not accepted by all classes of creditors and stockholders, and provisions to this effect are included in section 77. To approve a provision in a plan of reorganization by which a minority of a class of creditors or stockholders could effectively block the reorganization although the plan conformed to the requirements of the statute in all respects would, in our opinion, give such a minority a right not contemplated by the law, and, also, would be contrary to the intent if not the letter thereof.

The provision in the bondholders' committee plan to the effect that its plan shall not be confirmed until at least two-thirds of the holders of the debtor's first mortgage bonds accepted it, would seem to be in the same category as the provision in the James plan. With respect to the bondholders' proposal that the plan provide for the sale of the debtor's property in the event of the refusal of more than one-third of any other class of the debtor's creditors and stockholders to accept the plan, we are unable to accept the bondholders' argument that the

provision contained in clause (5) in the first paragraph of subsection (b) of the act to the effect that a plan may provide for the sale of all or any part of the property of the debtor, contemplates the equivalent of a foreclosure and judicial sale. In our opinion the provisions of subsection (e) [231] of the act, outlining the procedure to be followed in the event of a failure of confirmation of a plan, clearly shows that the Congress intended that reorganization should be accomplished through confirmation of a plan, or that the proceeding should be dismissed. The Commission should not approve the provision for sale of the debtor's property upon failure of acceptance of the plan. The plan approved by the Commission should provide that the plan shall be accepted and confirmed in accordance with the provisions of section 77.

Both the bondholders' plan and the James plan contemplates the formation of a reorganization committee with broad powers. No provision for such a committee is made in the debtor's plan, although it does provide that representatives of the bondholders' committee shall represent the members of that committee in the reorganization, and that the form and provision of the several indentures, bonds, stock certificates and other instruments in connection with the reorganization shall be first approved by the bondholders' committee.

It is recognized that it is impracticable to specify in detail the form and provisions of the various indentures, bonds, stock certificates and other in-

struments which must necessarily be executed in consummating the reorganization proceeding although the terms and provisions thereof are of great importance to those participating in the proceeding. For this reason the Commission should recommend that the plan provide for the formation of a committee, after approval of the plan by the Commission and the court, with power to determine, subject to the approval of the Commission, the form and provisions of the indentures, bonds, stock certificates and other instruments in connection with the carrying out of the plan. The committee also should have power, but only such power as necessary, to carry out the plan in accordance with [232] its provisions. The committee should consist of three members, one member of which should be nominated by the bondholders' committee, one by the Reconstruction Finance Corporation, Railroad Credit Corporation and A. C. James Company as a group, and one by the Western Pacific Railroad Corporation.

Under the foregoing recommendations, the plan of reorganization would provide as follows:

1. The immediate issue by the reorganized company of \$10,000,000 principal amount of 30-year first mortgage 4 percent bonds, \$19,716,040 principal amount of 50-year income mortgage 4 percent bonds, \$29,574,060 par value of noncumulative, 5 percent preferred stock (\$100 par value a share), and \$30,068,220 par value of common stock, (\$100 par value a share). The debtor's existing equip-

ment obligation would be assumed by the reorganized company.

2. The sale of the \$10,000,000 principal amount of new first mortgage bonds, the purchasers to receive 10 shares of the new common stock for each \$1,000 principal amount of first mortgage bonds purchased.

3. The creation and maintenance of a capital fund of not to exceed \$500,000 in any one year or \$1,000,000 at any time, to be accumulated out of available net income remaining after payment of fixed charges.

4. The creation and maintenance of a one-half of 1 percent sinking fund for the retirement of the new income bonds out of available net income remaining after the payment of fixed charges; payments into the capital fund, and payment of interest on the new income bonds.

5. The holders of the debtor's existing first mortgage bonds to receive in exchange therefor and for accrued unpaid interest thereon all of the new income bonds and preferred stock, and \$8,214,766 par value of the new common stock; and contingent rights [233] to subscribe for the purchase of the new first mortgage bonds.

6. The Reconstruction Finance Corporation, Railroad Credit Corporation and A. C. James Company, holders of the debtor's notes which are secured by the pledge of the debtor's general mortgage bonds, to receive in exchange therefor and for accrued unpaid interest thereon, \$11,853,454 par

value of new common stock, the stock to be distributed among them on the basis of the general mortgage bonds held by each creditor, and contingent rights to subscribe for the purchase of the new first mortgage bonds.

7. The Western Pacific Railroad Corporation, an unsecured creditor to receive in exchange therefor subscription warrants for the purchase at par of the new first mortgage bonds to be sold.

8. The formation of a committee with such power as may be necessary to carry out the plan, and to determine, subject to the approval of the Commission, the form and provisions of the indentures, bonds, stock certificates and other instruments in connection with the carrying out of the plan; the committee to consist of three members, one member to be named by the bondholders' committee, one by the Reconstruction Finance Corporation, Railroad Credit Corporation and A. C. James Company as a group, and one by the Western Pacific Railroad Corporation.

9. The plan to be accepted and carried out in accordance with its terms and the provisions of section 77 of the Bankruptcy Act.

10. The obligations of the debtor not specifically provided for to be paid by the debtor or the reorganized company or *the* assumed by the reorganized company.

11. The plan should be effective as of January 1, 1937.



Prior to the approval of the plan by the court, the Commission should fix maximum limits of allowances for fees and expenses which [234] are to be paid by the debtor or the reorganized debtor with the approval of the court, as incidental to the reorganization, upon the basis of representations theretofore made to it, and pursuant to appropriate petition of interested parties to the court, transmitted to the Commission in accordance with the provisions of paragraph 2(1) of the General Orders in Bankruptcy XLIX of the United States Supreme Court.

In view of the provisions of subsection (f) of section 77, the Commission, when a plan is finally adopted, should give consideration to the granting of such authorization for the issue of such securities as may be required and appropriate for the execution of the plan.

The Bureau of Finance recommends that the Commission find that the plan as recommended herein will meet with the requirements of subsections (b) and (e) of section 77 of the Bankruptcy Act, and will be compatible with the public interest.

The journal entries covering the necessary accounting adjustments should be submitted to the Commission for approval before they are recorded on the books of the debtor or of the reorganized company.

An appropriate certificate should be issued.

[Endorsed on first page]: Exceptions must be filed with Commission and copies served so as to reach all parties or their attorneys who appeared at the hearing or on brief on or before Aug. 23, 1937.

[Endorsed]: Filed Aug. 6, 1937. [235]

---

Interstate Commerce Commission

Finance Docket No: 10913

**THE WESTERN PACIFIC RAILROAD  
COMPANY REORGANIZATION.**

**REPORT AND ORDER OF INTERSTATE  
COMMERCE COMMISSION IN PROCEED-  
ING UNDER SECTION 77 OF THE BANK-  
RUPTCY ACT.**

Submitted, November 17, 1937.

Decided, October 10, 1938. [236]

Plan of reorganization of the Western Pacific Railroad Company, pursuant to section 77 of the Bankruptcy Act, as amended, approved.\*

Frank C. Nicodemus, Jr., for Western Pacific Railroad Company.

---

\*Previous report in this proceeding, 207 I.C.C. 793.

Robert E. Coulson, James B. Alley, C. C. McChord, C. M. Clay, W. Meade Fletcher, Jr., Daniel Willard, Jr., Robert T. Swaine, Orville W. Wood, H. C. McCollom, and Orrin G. Judd for interveners.

## REPORT OF THE COMMISSION

By the Commission:

Exceptions to the report proposed by our Bureau of Finance were filed by The Western Pacific Railroad Company, hereinafter called the debtor, by a committee for certain institutional bondholders, the A. C. James Company, the Railroad Credit Corporation, the Reconstruction Finance Corporation, and the Irving Trust Company, trustee under the debtor's general and refunding mortgage. The proceeding has been argued orally before us. Our conclusions differ somewhat from those of the Bureau.

The debtor, on August 2, 1935, filed a petition in the District Court of the United States for the Northern District of California, [237] Southern Division, stating that it was unable to meet its debts as they matured and that it desired to effect a plan of reorganization under the provisions of section 77 of the act of July 1, 1898, entitled "An Act to Establish a Uniform System of Bankruptcy Throughout the United States", as amended. The court, on the same day, made and entered an order approving the petition as properly filed, and among other things, authorizing and directing the debtor, pending further order of the court, to operate and

maintain the railroad and property of the debtor and to manage and conduct the debtor's business as a railroad company. Trustees were appointed on September 23, 1935, and their appointments were ratified by division 4 on October 30, 1935. 207 I.C.C. 793. Copies of the debtor's petition and the order thereon have been transmitted to us by the clerk of the court; and in like manner we have received lists of all known creditors and stockholders of the debtor, and copies of the orders of the court determining the time within which the claims of creditors might be filed or evidenced and dividing the creditors and stockholders into classes. These documents and other documents similarly received are now of record in the proceeding before us.

On February 8, 1936, the debtor filed a plan of reorganization with the court and us. Pursuant to the provisions of section 77(d) of the Bankruptcy Act, after due notice, we began public hearings upon the debtor's plan of reorganization on March 23, 1936. Two other plans for the reorganization of the debtor were filed during the proceeding; one on behalf of certain institutional bondholders on September 28, 1936, and the other on behalf of the A. C. James Company, a secured creditor of the debtor, on October 26, 1936. These parties intervened in the proceeding and were represented by counsel at the hearing. Other interveners, similarly represented, included the trustees under the mortgages, the Reconstruction Finance Corporation, and the Railroad Credit Corporation, secured creditors.

Hearings in this proceeding were closed on December 9, 1936, and briefs were filed on January 11, 1937.

**Location and General Description of the Property.**

The debtor owns or operates a total of 1,207.51 miles of standard-gage, steam railroad. The main lines extend 924.17 miles eastward from Oakland, Calif., to Salt Lake City, Utah, and north- [238] ward 111.81 miles from Keddle to Bieber, Calif., with operating rights over the Great Northern Railway, 46.38 miles, from Bieber to Hambone, Calif. The debtor also operates 4.2 miles of ferry service from Oakland to San Francisco, and 185.3 miles of second main track, of which 182.91 miles between Weso and Alazon, Nev., are owned by the Southern Pacific. This territory is known as the "Paired Track" district since the two lines are used as a double-track railroad by both companies. Various branch lines springing from the Oakland-Salt Lake City line are as follows:

Niles to San Jose, Calif.....	23.07 miles
Calpine Junction to Calpine, Calif.....	12.62
Hawley to Loyalton, Calif.....	12.79
Reno Junction to Reno, Nev.....	33.11
Burmester to Warner, Utah.....	15.52
Miscellaneous .....	21.79
<b>Total.....</b>	<b>118.90 miles</b>



Owned or Controlled and Jointly Affiliated  
Railroad Companies.

The debtor owns all the outstanding capital stock of the Sacramento Northern Railway, an electrically operated standard-gage, freight and passenger railroad, consisting of 276.2 miles of road serving and connecting San Francisco and Oakland with various Sacramento Valley cities, principally Pittsburg, Vacaville, Sacramento, Woodland, Marysville, Colusa, and Oroville, all in California.

By ownership of more than 99 percent of the outstanding capital stock, the debtor controls the Tidewater Southern Railway, which operates a standard-gage, steam freight line 61.38 miles in length, connecting Stockton with Manteca, Escalon, Modesto, and Turlock in the San Joaquin Valley of California.

The debtor owns all the outstanding capital stock of the Deep Creek Railroad Company, which owns and operates a standard-gage, steam railroad extending from Wendover to Gold Hill, Nev., a distance of 44.6 miles. In addition it owns 50 percent of the capital stock of the Salt Lake City Union Depot & Railroad Company;  $33\frac{1}{3}$  percent of the capital stock of the Central California Traction Company, operating an electrically operated freight railroad extending from Stockton to Sacramento, Calif., with a road mileage of 53.78 miles; and 50 percent of the capital stock of the [239] Alameda Belt Line, operating 15.86 miles of terminal switch-

ing line in the city of Alameda on San Francisco Bay.

None of the above subsidiary or affiliated companies has filed a petition under section 77 of the Bankruptcy Act, as amended.

### Corporate and Financial History.

The debtor was incorporated under California laws on June 16, 1916, and as of July 14, 1916, acquired the railroads and all other properties of the Western Pacific Railroad Company sold at foreclosure on June 28, 1916. Upon incorporation, the debtor had an authorized capital stock of \$75,000,000, consisting of 475,000 shares of common and 275,000 shares of preferred stock of the par value of \$100 each.

The debtor, by its first mortgage dated June 26, 1916, to the First Federal Trust Company and Henry E. Cooper, trustees (Crocker First National Bank of San Francisco and Samuel Armstrong, now successor trustees), authorized a maximum of \$50,000,000 of first-mortgage bonds to be at any time outstanding. A principal amount of \$20,000,000 thereof was issued and sold as a part of the 1916 plan of reorganization, at 90, producing \$18,000,000 in cash. Of this amount, approximately \$2,000,000, together with cash from receivers, was applied in defraying the expenses of incorporation, expenses incurred in connection with foreclosure and reorganization proceedings, and payment of the distributive shares of non-participating first-mort-

gage bondholders of the old company; and \$1,000,000 was retained as working capital. The balance of approximately \$15,000,000 was deposited under the debtor's first mortgage and applied to capital purposes as provided in the mortgage.

The debtor thus commenced operations with \$75,000,000, par value, of capital stock, and \$20,000,000 of its first-mortgage bonds outstanding. Additional bonds were not issued by the debtor until 1921, in which year \$4,180,000 of its first-mortgage bonds were sold at 85 and the \$3,553,000 realized was used to purchase the properties of the Sacramento Northern Railroad through the Sacramento Northern Railway. As of September 30, 1936, a total of \$49,290,100, face amount, of the debtor's first-mortgage bonds were outstanding, the additional bonds having been issued for the following purposes: \$3,000,000 in 1922 to retire outstanding equip- [240] ment-trust certificates; \$4,000,000 in 1925 for general capital purposes; \$2,600,000 in 1926 for general capital purposes; \$2,950,000 in 1927 in substitution of the \$3,000,000 issued in 1922 then outstanding in the aggregate amount of \$2,950,000; \$5,000,000 in 1929 for general capital purposes; \$572,800 in 1930 for purchase of San Francisco-Sacramento Railroad Company properties through the Sacramento Northern Railway; \$5,000,000 in 1930 for general capital purposes of the debtor and its subsidiary, the Sacramento Northern Railway; \$5,000,000 in 1931 and 1932 to finance in part construction and acquisition of the Northern

California extension; and \$645,000 in 1931 for general capital purposes. Interest on the bonds was paid as due until March 1, 1934. The interest payment due on that date was not paid, and no interest payment has since been made.

The debtor issued in 1931 and 1932, in addition to the above-mentioned \$5,000,000 of its first-mortgage bonds, \$5,000,000 of gold debentures, to finance the cost of its Northern California extension. These debentures were retired in 1932 through the issue of notes payable to the A. C. James Company for \$4,999,800 (\$200 being paid in cash), which notes were secured by \$6,249,500, face amount, of the debtor's general and refunding mortgage, series A, 5-per-cent gold bonds. The latter bonds were issued under the debtor's general and refunding mortgage, dated January 1, 1932, authorizing a maximum of \$100,000,000 of general and refunding bonds to be at any one time outstanding, but reserving \$49,292,300, principal amount, thereof for the purpose of refunding, paying, purchasing, redeeming, or otherwise acquiring the first-mortgage bonds then outstanding in that amount, and reserved \$5,000,000, principal amount, thereof against the outstanding debentures. The reserved bonds were issuable upon the retirement of the securities against which they were reserved. None of the debtor's general and refunding bonds have been sold, but \$18,999,500, principal amount, of such bonds have been nominally issued and are nominally outstanding solely as collateral to secure certain of the debtor's promissory

notes. Of these pledged bonds, \$10,750,000 are now pledged as part security for the debtor's promissory notes to the Reconstruction Finance Corporation, \$4,000,000 are pledged under its promissory notes to the Railroad Credit Corporation, and the remaining \$4,249,500 are still pledged under the A. C. James [241] Company note. The indebtedness to the Reconstruction Finance Corporation and the Railroad Credit Corporation was contracted in 1932 and 1933.

Prior to the date of trusteeship, the debtor created equipment-trust obligations in the total amount of \$13,400,000, of which \$637,000 was outstanding as of June 30, 1938. On that date there also remained unpaid \$229,265.50 on a conditional sale and lease of locomotives. All interest and principal payments on equipment trusts and the conditional sale lease have been met when due.

Subsequent to the date of trusteeship, by reports and orders of March 3 and October 15, 1936, January 25, 1937, and November 4, 1937, and by order of February 12, 1937, division 4 granted authority to the debtor's trustees to issue not exceeding \$13,000,000 of trustees' certificates, and to assume obligation and liability in respect to not exceeding \$2,320,000 of equipment-trust certificates. 212 I.C.C. 356; 217 I.C.C. 393, 395, and 777; and 224 I.C.C. 150. (The \$3,000,000 trustees' certificates authorized by the order of October 15, 1936, were for the purpose of refunding the \$3,000,000 trustees' certificates authorized by the order of March 5, 1936.)



The proceeds from the sale of those securities were to be used in the rehabilitation and improvement of the debtor's fixed plant and existing motive power and cars, and the acquisition of additional equipment. Under authority of the court, the trustees have initiated the rehabilitation program and it is now practically complete. Under our accounting rules such expenditures are chargeable in part to operating expenses. The inclusion of large amounts of normal operating expenses obviously reduces the amount of income available for interest and other fixed charges, and consideration should be given to this fact in studying the debtor's income accounts during periods when extraordinary expenditures were being incurred.

#### Present Financial Structure.

The trustees' balance sheet as of June 30, 1938, shows total assets of \$173,650,980.19. Investments included therein total \$165,785,843.99, including road and equipment \$143,447,447.51, sinking fund and deposits \$207,387.09, and miscellaneous physical property \$4,650,137.02. Investments in affiliated com- [242] panies pledged under the debtor's first mortgage amount to \$10,224,421.66, and consist of \$99,500.40 of capital stock of the Salt Lake City Union Depot & Railroad Company, \$999,500 of capital stock of the Sacramento Northern Railway, \$450,000 of capital stock of the Deep Creek Railroad Company, \$175,220.75 of capital stock of the Standard Realty & Development Company, \$3,-

975,456.13 of Sacramento Northern Railroad 5-percent 20-year gold bonds, and \$4,524,744.38 of notes receivable from the Sacramento Northern Railway. Investments in affiliated companies pledged under the debtor's general and refunding mortgage total \$3,159,061.78, and consist of \$1,223,848.94 of capital stock of the Tidewater Southern Railway Company, \$128,651.56 of common stock, \$264,715.47 of preferred stock, and \$270,375.50 of first-mortgage 5-percent gold bonds of the Central California Traction Company; \$465,600 of capital stock of the Alameda Belt Line, \$1,318.63 of capital stock of other companies, and \$804,551.68 of notes receivable from the Tidewater Southern Railway Company, Standard Realty & Development Company, and Deep Creek Railroad Company. Investments in affiliated companies unpledged amount to \$5,019,210.68, of which \$4,175,356.42 represent advances to the Sacramento Northern Railway, \$798,422.82 advances to other affiliated companies, \$5,500 represents capital stock of the Alameda Belt Line, and \$39,931.44 due from the Railroad Credit Corporation. Other investments amount to \$78,178.25 and consist principally of \$74,472.88 of advances to the Railway Equipment & Realty Company, Limited.

Current assets are shown in the amount of \$5,481,640.99, and comprise \$1,108,785.85 in cash, \$171,976.04 in special deposits, \$1,205,057.66 of traffic and car service balances receivable, \$156,068.64 of net balances receivable from agents and con-

ductors, \$548,913.37 of miscellaneous accounts receivable, \$3,140,625.85 of material and supplies, \$14,377.91 of interest receivable from affiliated companies, \$181,337.70 rents receivable, and other current assets of \$23,497.97.

Deferred assets are shown in the amount of \$317,418.69 and unadjusted debits in the amount of \$2,066,076.52. The latter item consists of \$5,541.17 of rents and insurance premiums paid in advance, \$1,051,067.23 of discount on funded debt, and \$1,009,468.12 of other unadjusted debits. [243]

Liabilities shown on the balance sheet of the same date, are capital stock, \$75,800,000, consisting of \$47,500,000 of common and \$28,300,000 of preferred stock. Government grants are shown at \$169,281.11, and total long-term debt is shown as \$68,926,004.44. Included in the latter item is \$50,147,365.50 of funded debt unmatured, consisting of \$49,290,100 of first-mortgage 5-percent gold bonds, \$637,000 of equipment-trust certificates, and \$220,265.50 due under the Baldwin Locomotive Works lease. The long-term debt includes also \$11,108,851.83 of receivers' and trustees' certificates, and \$7,669,787.11 of nonnegotiable debt to affiliated companies. Of this last item, \$7,609,370.43 is due the Western Pacific Railroad Corporation.

Total current liabilities are shown as \$26,316,674.89. They include \$2,445,609.88 of notes payable to the Railroad Credit Corporation, \$461,787.30 of traffic and car service balances payable, \$1,175,129.61 of audited accounts and wages payable, \$112,-

639.10 of miscellaneous accounts payable, and \$12,989,714.34 of interest matured unpaid. The latter amount consists of \$131,779.15 of interest on Railroad Credit Corporation notes, \$639,217.91 of interest on Reconstruction Finance Corporation notes, \$1,124,955 of interest on A. C. James Company notes, \$440 of interest on equipment-trust certificates, \$11,093,019.78 of interest on first-mortgage 5-percent gold bonds, and \$302 of interest on trustees' certificates. There also are included in the total current liabilities \$894,935 accrued unmatured interest, \$8,987.48 accrued unmatured rents, \$4,999,800 of notes payable to A. C. James Company, \$2,963,000 of notes payable to the Reconstruction Finance Corporation, \$3,000 trust certificates, and \$262,322.18 other current liabilities.

Total deferred liabilities are shown as \$19,521.96, and total unadjusted credits as \$11,334,893.42. The latter comprises \$433,529.54 of tax liability, \$6,890.25 of premium on equipment-trust certificates, \$10,811,559.91 of accrued depreciation on equipment, and \$82,913.72 of other unadjusted credits.

The above-mentioned liabilities total \$182,566,375.82. Two additional items totaling \$7,171,169.07, are described as a surplus-investment in road equipment and cash materials, and other property purchases, representing the value of Western Pacific Railway property purchased in excess of cash paid, and for value of capital [244] stock issued in exchange for same. This amount, added to the figure of \$182,566,375.82, produces the sum of \$189,737,544.89.

The balance sheet shows a deficit of \$16,086,564.70 in corporate surplus. This consists of appropriated surplus amounting to \$10,871,559.44 represented principally by additions to property through income and surplus, and an accumulated debit balance in profit and loss of \$26,958,124.14.

### Traffic and Revenue.

The main line of the debtor's railroad extending from Oakland, Calif., to Salt Lake City, Utah, forms an important part of a through route from the Pacific coast to Chicago, Ill., and other important Middle Western points. Fast through schedules are maintained by the debtor and the Denver & Rio Grande Western Railroad and Missouri Pacific Railroad Company, with which companies the debtor has close affiliations. Its line also connects with that of the Atchison, Topeka & Santa Fe Railway Company at Stockton, Calif., and with that of the Great Northern Railroad Company at Bieber, Calif., thus forming a link in a north and south route on the Pacific coast. The latter route is comparatively new, having been established in the latter part of 1931 by the construction of the debtor's line northward from Keddle to Bieber, known as the Northern California extension, and the extension of the line of the Great Northern southward from Klamath Falls, Oreg., to Bieber.

Although operations over the debtor's Northern California extension began in the depth of the depression, considerable traffic has moved over it from



the start. Traffic over this extension and revenue derived therefrom are considered separately from the debtor's other traffic and revenues. During the years 1924 to 1929, inclusive, the debtor and its subsidiary, the Sacramento Northern Railway, had an agreement with the Southern Pacific Company for the transportation for the Southern Pacific of certain carload traffic between Chico, Calif., and Weso, Nev., at the rate of \$60 per car, of which the debtor received \$54 per car. This agreement was terminated at the end of 1929, and since the tonnage moved under agreement and the revenue therefrom were large, the statistical data shown below relating to the debtor's traffic have been adjusted by excluding the freight moved under that agreement. [245]

The freight traffic handled and the freight revenue received by the debtor in the years 1923 to 1935, inclusive (traffic and revenue of subsidiaries will be discussed hereinafter), excluding traffic and revenue under the Chico-Weso Bridge agreement and that handled via the Northern California extension, were as follows:

Year	Cars	Tons	Revenue	Revenue per ton	Percent of increase or decrease over or under preceding year	
					Tons	Revenue
1923	96,531	2,875,108	\$10,513,355	\$3.66	—	—
1924	98,297	2,854,602	10,562,340	3.69	—0.7	—0.5
1925	113,633	3,198,214	11,736,434	3.67	+12.0	+11.1
1926	120,545	3,326,637	12,252,189	3.68	+4.0	+4.4
1927	121,071	3,486,668	12,697,985	3.64	+4.8	+3.6
1928	124,110	3,567,798	13,887,953	3.89	+2.3	+9.4
1929	124,181	3,616,927	14,287,250	3.95	+1.4	+2.9
1930	131,242	3,776,046	13,796,125	3.65	+4.4	—3.4
1931	106,321	3,070,577	11,078,891	3.61	—18.7	—19.7
1932	83,549	2,330,505	8,558,209	3.67	—24.1	—22.8
1933	83,957	2,359,810	8,520,315	3.61	+1.3	—0.4
1934	93,115	2,616,182	9,173,115	3.51	+10.9	+7.7
1935	92,902	2,489,273	9,910,386	3.98	—4.9	+8.0

Agricultural and manufactured and miscellaneous products comprised the greater part of the traffic moving over the debtor's line from Salt Lake City to Oakland. In the period 1928 to 1935, inclusive, for example, of the total carloads of commodities carried, manufactured and miscellaneous products constituted  $33\frac{1}{3}$  percent, and agricultural products  $33\frac{1}{3}$  percent. Forest products accounted for 7.5 percent, mineral products  $19\frac{2}{3}$  percent, and animal products 6 percent. Of the total freight revenue received from the transportation of this freight, approximately 40 percent was derived from manufactured products, 28 percent from agricultural products, 5 percent from forest products, 13.5 percent from mineral products,  $5\frac{2}{3}$  percent from animal

products, and the remainder from less-than-carload freight.

The above tabulation shows that the debtor's freight traffic in 1930, amounting to 3,776,046 tons, was the greatest for any of the years. There was moved an average of 2,573,269 tons in the following five years, 1931-35, inclusive, a decrease of 32 percent as compared with 1930. During the same period, agricultural products transported declined 20 percent, animal products 16.7 percent, mineral products 42.2 percent, forest products 44.4 percent, manu- [246] factured products 28 percent, and less-than-carload freight 29.7 percent, as compared with 1930.

Freight carried in 1935 amounted to 2,489,273 tons, a decrease of 35 percent under 1930. In 1935, traffic in agricultural products declined 25.1 percent, animal products 27.9 percent, mineral products 51.4 percent, forest products 45.6 percent, manufactured products 20.6 percent, and less-than-carload freight 20.8 percent under 1930:

Revenue from freight in 1930 amounted to \$13,796,125. During the period 1931-35, inclusive, freight revenue averaged \$9,448,183, a decline of 32.3 percent as compared with 1930. In the same period revenue from agricultural products declined 29.3 percent, animal products 20.8 percent, mineral products 60.9 percent, manufactured products 31.1 percent, and less-than-carload freight 28.2 percent.

Freight revenue amounted to \$9,910,386 in 1935, a decrease of 28.9 percent as compared with 1930.

In 1935, revenue received from agricultural products decreased 28 percent, animal products 34.7 percent, mineral products 43.4 percent, forest products 40.3 percent, manufactured products 19.6 percent, and less-than-carload freight 37.2 percent under 1930.

Forty-three percent, or 1,637,984 tons, of the debtor's freight traffic in 1930 consisted of traffic interchanged with the Denver & Rio Grande Western, Oregon Short Line, and Union Pacific. During the period 1931-35, inclusive, traffic interchanged with those lines averaged 1,196,971 tons, or a decrease of 20 percent under 1930. For the year 1935, traffic interchanged with the same lines amounted to 1,381,186 tons, or a decrease of 15 percent under 1930. It should be noted also that for many years the debtor was dependent upon connections for the greater part of its traffic, and, although to a less degree than formerly, it still receives more than one-half of its total freight from connecting carriers, and approximately one-third of it is received from and delivered to connections.

The debtor estimates that the revenue from freight moving over its line from Oakland to Salt Lake City will amount to \$10,084,951 in 1936, \$10,857,252 in 1937, \$11,629,553 in 1938, \$12,518,672 in 1939, and \$13,747,996 in 1940. The latter amount is an increase of \$3,837,610, or 38.7 percent, over 1935 revenue, and approximately equals that received in 1930. [247]

Freight moved over the Northern California extension in 1932 amounted to 340,107 tons, and \$1,098,016 in revenue was derived therefrom. In the year 1933, tonnage and revenue amounted to 396,862 tons and \$1,491,466 revenue, in 1934 to 596,378 tons and \$2,119,427 revenue, and in 1935 to 639,980 tons and \$2,289,858 revenue. The principal commodities carried consisted of forest, manufactured, and agricultural products. The debtor estimates that revenue from freight moved over this line will amount to \$2,550,524 in 1936, \$2,973,750 in 1937, \$3,406,978 in 1938, \$3,819,559 in 1939, and \$4,171,625 in 1940. The latter amount is an increase of \$1,881,767, or 82 percent, over 1935 revenue.

Total revenue to be derived from freight in the period 1936 to 1940, inclusive, is estimated by the debtor to amount to \$12,635,475 in 1936, \$13,831,002 in 1937, \$15,036,531 in 1938, \$16,338,231 in 1939, and \$17,919,621 in 1940. Compared with 1935, these amounts represent an increase of 3.5 percent in 1936, 13.3 percent in 1937, 23.3 percent in 1938, 33.9 percent in 1939, and 46.8 percent in 1940.

A witness for the debtor testified that the increased revenues estimated for the future were based on expected increases in traffic and freight rates. He further testified that the drastic decline in revenues recently suffered by the debtor resulted not only from the business depression but also from intense competition from water and motor carriers.

The debtor and other lines with which it has joint freight rate arrangements have water competition



via the Panama Canal between the Pacific coast and Atlantic and Gulf ports, as well as in connection with canal lines and inland waterways. There is also strong competition coastwise between California and Washington. It was the opinion of the debtor's witness that increased operating expenses would compel water carriers to increase rates and thereby would divert traffic to railroads. The witness also was of the opinion that railroad freight rates, as a whole, are as low as they will be for a number of years, and the tendency in the immediate future will be towards a higher level of rates.

This witness stated that prior to the advent of motor truck competition, practically all the debtor's traffic between California and Utah moved under class rates, which for the first four classes were \$2.165, \$1.845, \$1.625, and \$1.35 per 100 pounds between San Francisco and Utah common points. Motor truck competition [248] made it necessary for the debtor to publish pick-up and delivery rates of \$1 and \$1.25 per 100 pounds on a great many commodities, and today at least 90 percent of such traffic of the debtor moves under the reduced rates. It was his opinion that effective regulation of motor carriers would tend to divert traffic to the railroads.

Passenger, mail, express, and other related revenues received by the debtor in the years 1923 to 1935, inclusive, were as follows:

Year	Revenues	Year	Revenues
1923	\$3,250,677	1930	\$1,738,884
1924	2,891,137	1931	1,288,093
1925	2,697,899	1932	645,760
1926	2,515,900	1933	433,959
1927	2,350,320	1934	457,481
1928	2,217,421	1935	559,816
1929	2,135,828		

It thus appears that such revenues steadily declined from 1923 to 1934, the decrease amounting to 79.7 percent between 1923 and 1933. In 1935 such revenues had increased 22.5 percent over 1933, but were still 73.8 percent below those for 1923. The debtor estimates that revenues from these sources will amount to \$654,710 in 1936, \$1,063,058 in 1937, \$1,299,060 in 1938, \$1,860,815 in 1939, and \$1,535,372 in 1940. At the time of the hearing the debtor expected to inaugurate additional passenger service between San Francisco and Salt Lake City in May, 1937, only one passenger train daily between those points having been operated since April 24, 1932. By shortening of schedules and with greater advertising of the improved service of the Denver & Rio Grande Western via the Dotsero Cut-off, one of the most scenic routes between California and the East, passenger revenues should be increased materially.

The debtor filed a forecast showing that total railway operating revenues would amount to \$13,438,342 in 1936, \$15,053,934 in 1937, \$16,507,579 in 1938, \$18,383,490 in 1939, and \$19,654,935 in 1940.

As a bridge line to and from the Pacific coast the debtor's railroad may, as a result of the completion of the Dotsero Cut-off in 1934, come into greater use. The railroad distance between Denver and Salt Lake City and points east of the former and west of the latter is greatly shortened by use of this Cut-off and the Moffat Tunnel. The rehabilitation program of the debtor's road now in [249] progress and the betterment of its equipment should enable it to give improved service. As a consequence, the debtor and the lines with which it is closely affiliated should be in better position to compete with the Southern Pacific and Union Pacific for transeontinental traffic. Increased traffic over its Northern California extension reasonably may be expected. Greater through and local traffic should result from a further revival in general business conditions. Whether revenues in the future will reach the level estimated by the debtor for 1940, is open to doubt. To the extent that the debtor relies upon increased freight rates, and a recovery of the traffic lost to competing forms of transportation under present State and Federal regulatory conditions, its estimates rest upon uncertainties.

#### *Traffic and Revenue of Subsidiaries.*

The main line of the Sacramento Northern Railway, separately operated, extends from Oakland to Chico, Calif., and both freight and passenger services are rendered over it. Its freight traffic consists

largely of agricultural, manufactured and miscellaneous, and mineral products.

Freight traffic and revenue derived therefrom for the years 1930 to 1935, inclusive, were as follows:

Year	Tons	Revenue
1930	840,306	\$1,234,696
1931	743,220	971,482
1932	629,792	769,412
1933	649,554	717,435
1934	704,472	760,033
1935	697,464	760,528

A witness for the debtor testified that the decline in traffic was occasioned by competition of motor trucks, depressed economic conditions, and the displacement of coal by oil and natural gas. It was his opinion, however, that the Sacramento Northern's freight earnings in the future should increase materially from an improvement in the market demand for California fruits and vegetables, and that improved facilities recently had been made available to the carrier's shippers. He further testified that general business conditions were improving and that the carrier was in a better position to meet truck competition. The witness was of the opinion that the carrier's [250] gross revenues from transportation and other railway operations would amount to \$1,322,676 in 1936, \$1,417,458 in 1937, \$1,528,492 in 1938, \$1,616,891 in 1939, and \$1,689,038 in 1940. The latter amount is a 38.3 percent increase over gross revenues for 1935, and is approximately

\$40,775 greater than the actual gross revenue for 1931, but is approximately \$394,000 less than the actual for 1930.

The main line of the Tidewater Southern Railway extends from Stockton to Hillmar, Calif., serving a territory predominantly agricultural. The carrier's freight traffic consisted principally of agricultural products and manufactured and miscellaneous commodities.

Freight traffic and revenue derived therefrom for the years 1930 to 1935, inclusive, were as follows:

Year	Tons	Revenue
1930	199,607	\$425,596
1931	227,856	264,796
1932	249,820	230,450
1933	255,833	202,434
1934	266,274	271,519
1935	211,264	272,299

A witness for the debtor testified that the Tidewater Southern's total railway operating revenues would amount to \$287,136 in 1936, slightly higher than those in 1935, but that since the small area served by the line does not afford much opportunity for increased acreage production, earnings are not expected to increase materially in the future.

The Deep Creek Railroad Company operates 44.6 miles of line south from Wendover, Utah, serving a territory devoted principally to mining. Its freight revenues are dependent largely on mining activities in the Gold Hill District at the southerly terminus



of the line, although some revenue is derived from the movement of sheep to winter ranges in the fall and out in the spring.

A witness for the debtor testified that the revenues of this line have in the past few years been nominal, but with a revival in mining it is possible for a traffic to develop which would increase materially the revenue. For example, in 1923 revenues were \$42,385, in 1924 \$71,670, and in 1925 \$40,268. In 1934 and 1935, however, they were only \$7,383 and \$5,355, respectively. For the next several years revenues are not expected to increase. [251]

#### Earnings Available for Charges.

The reported consolidated net income of the debtor's system available for payment of interest on funded debt for the years 1926-35, inclusive, was \$4,759,282 in 1926, \$2,674,494 in 1927, \$2,964,371 in 1928, \$2,529,846 in 1929, \$1,552,487 in 1930, \$186,708 deficit in 1931, \$252,706 in 1932, \$674,007 in 1933, \$1,084,244 in 1934, and \$805,589 in 1935. Operating ratio percentages for the same years were, respectively, 70.3, 79.2, 80.3, 83.2, 84, 91, 85.8, 83, 81.1, and 83.7.

It would appear from the record, however, that before the foregoing amounts may be considered indicative of future earnings, certain factors should be taken into consideration. It was testified, for example, that a substantial amount of deferred maintenance had been permitted to accrue on the debtor's property by 1927. Beginning in that year

and continuing into 1931, considerable sums were expended yearly in an effort to overcome existing deferred maintenance. This program of rehabilitation was discontinued in 1931 by reason of drastically declining revenues, and it was testified that approximately \$5,000,000 of deferred maintenance existed in the debtor's property at the end of 1935. Although the witnesses were unable to allocate any specific amount for undermaintenance to particular years, it is reasonably certain that maintenance was deficient during the years 1930 to 1935, inclusive. Total system maintenance expenditures for the years 1922 to 1935, inclusive, were \$73,673,799, and total system operating revenues were \$219,808,043. By dividing total maintenance expenditures, plus the \$5,000,000 of deferred maintenance, by total operating revenues, a ratio of 35.79 percent results which may, for the purposes of this proceeding, be considered as normal for the period. If this ratio is applied to the operating revenues for the years 1931 to 1935, inclusive, and the resulting amounts are substituted for the amounts reported for maintenance expenditures in those years, the deficit in income reported available for interest for 1931 would be increased \$263,231, and the amounts reported for 1932 would be decreased \$692,282, for 1933 \$408,488, for 1934 \$843,627, and for 1935 \$585,633. If such adjustments are made, however, the results should be further adjusted by adding \$122,735 for 1931, \$161,286 for 1934, and [252] \$436,036 for 1935, since those amounts were re-

ported expended in those years for rehabilitation and improvements.

To be indicative of probable future earnings, further adjustments should also be made. The amounts reported as income available for interest reflect amortization of discount on funded debt of \$139,698 in 1931, \$144,911 in 1932, \$146,878 in 1933, \$144,063 in 1934, and \$143,433 in 1935. Since the reorganized company's income would not be affected by such items, those amounts should be credited to the income reported in those years. The income reported for 1934 and 1935 should also be adjusted for the \$97,683 accrued by the debtor for railroad retirement in 1934 and credited in 1935. The report of our Bureau of Accounts also shows that deductions of \$279,946 in 1931, \$98,696 in 1932, and \$333,408 in 1933, and a credit of \$17,057 in 1934, should be made for improper accounting.

If the foregoing adjustments were made, the consolidated system income available for interest for the years 1931 to 1935, inclusive, would be \$467,000 deficit in 1931, \$393,000 for deficit in 1932, \$80,000 in 1933, \$661,000 in 1934, and \$702,000 in 1935, or an average of \$116,600 per annum for the period. It is true that such amounts would not reflect probable increased earnings from the debtor's Northern California extension, calculated by the debtor at \$500,000 per annum if operations over the line had become seasoned. On the other hand, they do not reflect present social security and railroad retirement

taxes on a retroactive basis, nor increases in wages or prices since the hearing.

For the year ended December 31, 1936, the debtor reported total system operating revenue of \$16,547,344 and total system operating expenses of \$14,449,275, of which \$1,585,530 was attributed to the current rehabilitation program. If the latter expenses, as well as \$135,401 for amortization of discount on funded debt, be eliminated, the income available for interest would be \$1,902,033, as compared to the \$181,102 actually reported. For the year ended December 31, 1937, the debtor reported total system operating revenue of \$17,918,485, and total system operating expenses of \$16,987,490, of which \$1,837,495 was attributed to the current rehabilitation program. Eliminating the latter and the item of \$135,401 reported for amortization of discount on funded debt, the income available for interest for the period would be \$1,069,785 instead of the reported deficit of \$903,112. [253]

In statements filed in this proceeding the debtor estimated that total operating revenues of its system for the years 1936-40, inclusive, would be \$15,050,200, \$16,761,200, \$18,325,200, \$20,288,200 and \$21,632,000, respectively. Excluding operating charges incident to its current rehabilitation program, it estimated that consolidated income available for interest would be \$1,521,386 in 1936, \$2,180,585 in 1937, \$2,738,886 in 1938, \$3,365,836 in 1939, and \$3,769,836 in 1940, or an average of \$2,715,306 for the period. Operating ratios estimated for the same years were, respectively, 79.28, 76.01, 73.56,

72.28, and 75.6, and expenditures incident to its current rehabilitation program were estimated at \$1,747,384 in 1936, \$2,021,312 in 1937, and \$1,280,074 in 1938.

These estimates were based on assumed revenues, previously analyzed, and assumed operating ratios, which are influenced greatly by operating revenues. It is significant that the estimates were based, among other things, upon the assumption that there would be increases in rates but that there would be no increases in operating costs, either through prices of material or wages. The estimates also ignored necessary deductions for the creation and maintenance of the various funds proposed under the debtor's plan. It is reasonably certain that some traffic diverted to motor carriers in recent years will not be regained. Strenuous competition must be expected not only from those carriers, but from water carriers and, especially, from other strong railroads serving the same territory as the debtor. This latter competition compels the movement of trains on schedule regardless of the load. Long stretches of the territory through which the debtor's road extends are sparsely populated and productive of little or no traffic. The debtor's volume of traffic is subject to wide fluctuations, and the topography of the country entails expensive helper service over high summits.

Although the 1936 adjusted income available for interest exceeded the debtor's estimate, it is significant to note that the amount reported for 1937,



when adjusted, was \$832,248 less than the adjusted amount reported for 1936, and \$1,110,801 less than the debtor's estimate for 1937. The decrease in income available for interest occurred despite the large increase in operating revenues in the 1937 period over the 1936 period. The decreased income is undoubtedly accounted for by reason of increased costs. [254] We have heretofore stated that the debtor's forecast of future earnings was based on assumed increases in rates but no increases in costs. The results for 1937 clearly demonstrate the fallacy of the latter assumption. The results of operation reported for the first six months of 1938 cast further doubt upon the accuracy or trustworthiness of the debtor's estimate of future earnings. For those months there was a deficit of \$1,120,403, in available income, after adjustment similar to that made in 1936 and 1937, in the system's consolidated income available for interest. It is true that ordinarily the debtor's earnings are much greater in the last six months than the first six months of the calendar year. However, the results for the 12 months, July, 1937, to June, 1938, show a deficit of \$264,000 in the system's consolidated income available for interest. A consideration of these recent data (reported subsequent to the preparation of the debtor's estimate), together with other data of record, convinces us that too great reliance may not be placed upon the debtor's estimate of future earnings, and that the capital structure of the reorganized company must be conservative.

### Value for Rate-making Purposes.

Under section 19a of the Interstate Commerce Act, this Commission, by division 1, in *Western Pacific Ry. Co.*, 29 Val. Rep. 239, reported the value for rate-making purposes of the property owned by the debtor to be \$63,321,000 as of June 30, 1914, excluding working capital. In other proceedings, we reported the value for rate-making purposes of the properties of the debtor's wholly owned subsidiaries, Sacramento Northern Railway, Tidewater Southern Railway Company, and Deep Creek Railroad Company, in the total amount of \$18,123,283, as of their respective valuation dates. If there be added to the above amounts the net costs of additions and retirements between valuation dates and December 31, 1935, the total would be \$139,600,455.

### Classes of Creditors and Stockholders.

Pursuant to section 77(g)(7) of the Bankruptcy Act, the district court entered an order, on August 20, 1935, dividing creditors and stockholders, for the purposes of the plan and its [255], acceptance, into the following classes: Class 1, first-mortgage bonds; class 2, general and refunding bonds; class 3, debtor's secured promissory notes to the A. C. James Company; class 4, debtor's secured promissory notes to the Reconstruction Finance Corporation; class 5, debtor's secured promissory notes to the Railroad Credit Corporation; class 6, equipment obligations to the Baldwin Locomotive Works (assigned to Fidelity-Philadelphia Trust Company, trustee); class 7, equipment-trust certificates un-

der agreement of March 1, 1923; class 8, equipment-trust certificates under agreement dated March 15, 1924; class 9, equipment-trust certificates under agreement dated May 1, 1929; class 10, debtor's obligations as to advances made on open account by the Western Pacific Railroad Corporation; class 11, debtor's obligations as to advances made on open account by the Western Realty Company; class 12, debtor's preferred stock; class 13, debtor's common stock; class 14, all other claims, obligations, and liabilities not hereinbefore specifically described.

As recorded on the trustees' balance sheet of June 30, 1938, class 1 items consisted of \$49,290,100, principal amount, of first-mortgage 5-percent bonds, on which accrued and unpaid interest amounted to \$11,914,521; class 2 items consisted of \$18,999,500, principal amount, of general and refunding mortgage 5-percent bonds, entirely pledged as collateral for certain of the debtor's notes; class 3 items consisted of \$4,999,800, face amount, of notes to the A. C. James Company, on which accrued and unpaid interest amounted to \$1,124,955, and which are secured by \$4,249,500, principal amount, of the debtor's general and refunding bonds, and a second lien upon \$2,000,000, principal amount, of the same issue of bonds held by the Railroad Credit Corporation; class 4 items consisted of \$2,963,000, face amount, of notes to the Reconstruction Finance Corporation, on which accrued and unpaid interest amounted to \$649,181, the notes being secured by \$10,750,000, principal amount, of the debtor's gen-

eral and refunding bonds, and voting trust certificates for half of the voting stock of the Denver & Rio Grande Western Railroad Company, and a second lien upon \$2,000,000; principal amount, of the same issue of bonds held by the Railroad Credit Corporation; class 5 items consisted of \$2,445,610, face amount, of notes to the Railroad Credit Corporation, on which accrued and unpaid interest amounted to [256] \$135,296, which notes are secured by \$4,000,000, principal amount, of the debtor's general and refunding bonds, and a second lien upon the security held by the Reconstruction Finance Corporation, an assignment of certain advances by the Western Pacific Railroad Corporation, and an assignment of the distributive share of the debtor under the marshaling and distributing plan, 1931; class 6, 7, 8, and 9 items consisted of various equipment obligations aggregating \$857,265; class 10 items consisted of \$5,766,309; principal amount, of advances to the debtor by the Western Pacific Railroad Corporation, on which accrued and unpaid interest amounted to \$1,843,061; class 11 items consisted of \$50,000, principal amount, of advances to the debtor by the Western Realty Company, on which unpaid interest amounted to \$10,417; class 12 items consisted of \$28,300,000, par value, of the debtor's preferred stock; class 13 items consisted of \$47,500,000, par value, of the debtor's common stock; and class 14 items consisted of various other claims not specifically described by the court.

The proceeds from the loans comprising class 3, 4, and 5 items were applied by the debtor in partial

payment of the cost of constructing its Northern California extension, for payment of interest on its first-mortgage bonds and equipment obligations, miscellaneous capital expenditures, payment of taxes, and for advances to subsidiary railroad operating companies.

#### *Proposed Plans of Reorganization.*

The capital structures proposed for the reorganized company in the three plans filed, in the debtor's plan, if modified in accordance with the debtor's suggestions during the hearing and on brief; the distribution of the new securities to be issued under the plans; and the main features thereof, are summarized below.

Existing equipment obligations would not be disturbed under any of the plans. As filed, the debtor's plan would become effective as of January 1, 1936. The debtor later suggested January 1, 1937, as the effective date, that being the effective date of the other plans.

The plan of reorganization originally submitted by the debtor contemplated an initial issue of \$25,675,900 of new first-mortgage 4-percent bonds, \$41,774,796 of new 5½-percent income mortgage [257] bonds (cumulative for the income period in which such interest is payable and for the four income periods next succeeding the income period in respect to which such interest is payable), of which \$20,887,398 would be series-A bonds, and \$20,887,398 would be series-B bonds, \$8,092,709 of new non-cumulative junior lien 6-percent income bonds, or a



total of \$75,543,405, principal amount, of bonds. The plan further provides that 926,622 shares of new no-par common stock be authorized, of which 300,000 shares would be issued forthwith, and 626,622 shares would be reserved for issue upon conversion of \$20,887,398 of the new income bonds.

Under the debtor's plan, its existing first-mortgage 5-percent bonds would be exchanged on the basis of 30 percent in the new first-mortgage 4-percent bonds, and 70 percent in new income mortgage 5½-percent bonds plus additional income bonds equal in face amount to the unpaid interest. Ten million dollars of the new first-mortgage 4-percent bonds would be sold at par to the Reconstruction Finance Corporation to provide new money for the reorganized company. In consideration of that purchase, the Reconstruction Finance Corporation would receive for its claim against the debtor treatment equivalent to that given to the holders of the existing first-mortgage bonds.

The new junior lien income 4-percent bonds would be issued to the Railroad Credit Corporation and A. C. James Company in settlement of their claims, each to receive new bonds equal in face amount to the principal of the claim plus unpaid interest.

All the new stock would be placed in a voting trust under which three voting trustees nominated by the debtor and approved by the bondholders' committee would act pursuant to a voting trust agreement which would be acceptable to the debtor and the bondholders' committee. The voting trust would con-

tinue until 10 years from the date of confirmation of the plan. A majority of the debtor's board of directors would be nominees of the holders of income bonds, and as long as the Reconstruction Finance Corporation holds more than \$500,000 of the first-mortgage bonds, the voting trustees would elect to the board of directors a person designated or nominated by that corporation. In respect to the 300,000 shares of common stock immediately issuable under the plan and to the shares which may be issued on conversion of the income bonds [258] voting trust certificates would be issued. The certificates for 150,000 shares of the common stock would be placed in escrow with the trustee of the income mortgage and would be transferred to the holders of income mortgage bonds at \$27.50 per share if, commencing April 1, 1941, full interest was not paid on the income bonds in respect to the next preceding income period.

The debtor's plan further provided that there be created a contingency reserve fund of \$500,000 to be made available for the purpose of paying fixed interest charges, principal of and dividends on equipment obligations and operating expenses which could not otherwise be provided for without, in the opinion of the board of directors, unduly impairing free working capital. The fund would be created initially from the proceeds of the \$10,000,000 of new first-mortgage bonds to be sold in the reorganization, and thereafter maintained out of the net income remaining after the payment of fixed charges.

There would be created also out of available net

income before the payment of interest on income bonds a capital fund to be applied for capital investments made in the calendar year in which the fund is set aside, and no additional securities would be issued against such expenditures. The amount set aside in the capital fund for any calendar year would not exceed \$500,000 per year during the years 1936 to 1940, inclusive, \$1,000,000 per year during the years 1941 to 1945, inclusive, and in all subsequent years not more than 3 percent of gross revenues.

Provision for a sinking fund in an amount not exceeding in any calendar year one-half of 1 percent of the principal amount of the new income bonds, series A, also is made in the plan. The fund would be created and maintained out of net income remaining after payment of fixed charges, maintenance of the reserve fund, capital fund, and interest payments on income bonds, and would be applied to the redemption of the series-A income bonds.

The debtor's plan also provides for an additional interest fund to be created and maintained out of net income remaining after payment of fixed charges, payments in respect to the reserve fund and the capital fund, and interest on income mortgage bonds and junior lien bonds. The fund would not exceed one year's interest on all outstanding first-mortgage bonds and would be available only for the payment of interest on such bonds. [259]

During the hearing and on brief, counsel for the debtor suggested that the debtor's plan be modified

by providing that (1) the rate of interest on all bonds be 4 percent per annum, (2) there be created sinking funds of not less than one-half of 1 percent or more than 1 percent for the redemption of all bonds, (3) the escrow agreement with respect to the 150,000 shares of common stock be modified so that there would not be a peremptory forfeiture on the due date of interest, because such interest may be paid in cash out of the available net income of the next four income periods, and be further modified so that there would be no forfeiture at all if the failure to earn interest were caused by excessive maintenance or undue capital expenditures, (4) the voting trust be eliminated from the plan, and (5) there be issued \$7,245,274, par value, of 4-percent non-cumulative preferred stock to the Western Pacific Railroad Corporation and the Western Realty Company.

With the effective date of the plan as of January 1, 1937, the plan, modified as suggested, would provide for the initial issue of \$25,675,900, principal amount, of new first-mortgage 4-percent bonds, \$45,219,530, principal amount, of new income mortgage 4-percent bonds, \$8,386,040, principal amount, of new junior lien income 4-percent bonds, or a total of \$79,281,470 principal amount, of bonds \$7,245,274, par value, of new 4-percent preferred stock, and 300,000 shares of no-par common stock.

Subsequent to the issue of the report proposed by our Bureau of Finance, counsel for the debtor suggested on brief in support of exceptions to the report that the debtor's plan be modified further by

providing that the reorganized company issue \$19,858,020, principal amount, of new first-mortgage 4-percent bonds, \$39,432,100, principal amount, of new income 4-percent bonds, \$10,487,707, principal amount, of 15-year income notes to be secured by \$18,999,500, par value, of new prior-lien 4-percent preferred stock, \$9,503,664, par value, of new 4-percent participating preferred stock, \$7,188,607, par value, of new junior 4-percent convertible preferred stock, and 300,000 shares of new no-par-value common stock. Under the proposed modifications, existing first-mortgage bondholders would receive new first-mortgage bonds for 20 percent of the principal of their bonds, new income bonds for the remaining 80 percent, and new prior-lien preferred stock for accrued interest. The present holders of secured notes would receive new 15-year [260] notes for the face value of their notes and presumably new prior-lien preferred stock for accrued interest. The unsecured creditors would receive new junior convertible preferred stock in settlement of their claims, and the holders of present capital stock would receive in exchange therefor all the new no-par-value common stock.

Under the bondholders' plan, the reorganized company would issue initially \$19,858,020, principal amount, of new first-mortgage 4-percent bonds, \$19,716,040, principal amount, of new income mortgage 5-percent bonds (cumulative against only 3 years' income), or a total of \$39,574,060, principal amount, of new bonds. The plan further proposes the issue of \$27,930,800, par value, of new participating 6-



percent preferred stock (cumulative only to the extent that dividends are earned), and not less than 339,995 shares, nor more than 489,995 shares, of new no-par common stock.

The existing first-mortgage 5-percent bonds would be exchanged on the basis of 20 percent in new first-mortgage 4-percent bonds, 40 percent in new income mortgage 5-percent bonds, and 40 percent in new participating 6-percent preferred stock, accrued interest also being commuted into the latter stock. As provided in the debtor's plan, \$10,000,000 of the new first-mortgage 4-percent bonds would be sold in order to provide new money for the reorganized company.

The claims of the Reconstruction Finance Corporation, Railroad Credit Corporation, and A. C. James Company would be converted into the new common stock (taken at \$100 per share) on the basis of the collateral pledged under the debtor's notes to those creditors. Such stock, amounting to 189,995 shares, would be deposited under an escrow agreement subjecting the stock to purchase warrants. The reorganized company would be entitled to purchase any of the certificates to be issued under the escrow agreement under certain terms. The certificates to be issued to the Reconstruction Finance Corporation could be purchased by the other two secured creditors, and those of the Railroad Credit Corporation by the A. C. James Company.

The Western Pacific Railroad Corporation would be allotted purchase warrants, entitling the holders

thereof to purchase on or before December 1, 1941, all or any part of the 189,995 shares of the new common stock at the price of \$62 per share, plus interest thereon at the rate of 4 percent per annum from January 1, [261] 1937. In addition to its option under the escrow agreement the Western Pacific Railroad Corporation would be granted, through issue to it of subscription warrants, the first opportunity to provide the \$10,000,000 of required new money, receiving therefor the \$10,000,000 new first-mortgage 4-percent bonds and 150,000 shares of the new common stock.

To the extent that the Western Pacific Railroad Corporation should fail to exercise the subscription warrants, the bondholders' plan provides that the new money be provided upon less favorable terms to the debtor by the Reconstruction Finance Corporation, Railroad Credit Corporation, and A. C. James Company; and to the extent that they, in turn, should fail to provide it, the plan provides that it be supplied upon still less favorable terms by the present first-mortgage bondholders.

The bondholders' plan further provides that control of a majority of the board of directors of the reorganized company be vested in the new preferred stock until the reorganized company shall have demonstrated its capacity to pay a continuous return on that stock. A contingency reserve fund and a capital fund similar in all respects to those proposed by the debtor are provided for in the bondholders' plan. It also provides for a one-half of 1 percent sinking

fund for the redemption of the new income bonds, but only after payment of fixed and other contingent charges and the payment of dividends on preferred stock.

On briefs in support of exceptions to the proposed report of our Bureau of Finance, the bondholders' committee proposed that its plan be modified (1) by eliminating the provision for the contingency reserve fund, (2) to make the sinking fund payable out of available net income before preferred dividends, but reduce it to an annual one-half of 1 percent fund instead of a 1-percent fund, (3) to clarify the provisions respecting the offering of new securities to provide new money, by providing that it be made to the unsecured creditors or their assignees proportionately to the amounts of their respective claims, (4) to include in the escrow certificates to be delivered to the Reconstruction Finance Corporation and the Railroad Credit Corporation for their notes, express provisions that their acceptance shall not prejudice the rights of the Reconstruction Finance Corporation or the Railroad Credit Corporation against collateral which has been delivered by third persons to [262] secure the obligations of the debtor and which does not itself constitute a claim against the debtor or the debtor-property, (5) to provide that the reorganization committee shall be constituted of such number of members, not more than five, as we may determine, but that a majority of whom shall be elected by the bondholders in any manner which we may prescribe, and (6) to elim-

inate the provisions requiring the consent of two-thirds of the bondholders to the confirmation of the plan, but extend the provision for protecting a dissenting class through a judicial sale at a fair upset price to include the bondholders as a class.

The plan submitted by the A. C. James Company proposes that the reorganized company issue initially \$10,000,000, principal amount, of new first-mortgage 4-percent bonds, \$49,290,100, principal amount, of new general-mortgage 4 percent income bonds (cumulative only to the extent that interest is earned), and \$10,450,263, principal amount, of new noncumulative 4-percent debentures (convertible into 150 percent of their principal amount in 6 percent preferred stock), or a total of \$69,740,363, principal amount, of new bonds and debentures. The preferred stock of the debtor, of which \$28,300,000, par value, is now outstanding, would be delivered to the debtor under this plan, and \$5,807,650, par value, of such stock would be reissued. The common stock of the debtor, now outstanding of the par value of \$47,500,000, would be delivered to the debtor and be reissued.

The existing first-mortgage 5-percent bonds would be exchanged for the new general-mortgage 4-percent income bonds, with a bonus of \$500, par value, of common stock for each \$1,000 bond. The new noncumulative 4-percent debentures would be allotted to the Reconstruction Finance Corporation, Railroad Credit Corporation, and A. C. James Company, and those creditors would be given also a

bonus of \$500, par value, of common stock for each \$1,000 of the debtor's notes owned by them: The \$5,807,650, par value, of preferred stock would be issued to the Western Pacific Railroad Corporation and the Western Realty Company in settlement of the principal amount of their claims against the debtor.

Under this plan all accrued interest upon all outstanding debt would be canceled. [263]

The \$10,000,000, principal amount, of new first-mortgage bonds would be sold to provide new money for the reorganized company and the Western Pacific Railroad Corporation would be given the first right to purchase such bonds, with a bonus at the rate of 15 shares of the common stock for each \$1,000 first-mortgage bond purchased.

No reserve capital or sinking funds are provided for under the James plan.

The A. C. James Company also proposed modifications of its plan on brief in support of exceptions to the report proposed by our Bureau of Finance. Under the proposed modifications, the reorganized company would issue \$9,623,202, par value, of non-cumulative 5-percent preferred stock for unpaid interest on the present first-mortgage bonds, and on the claims of the Reconstruction Finance Corporation, the Railroad Credit Corporation, and the A. C. James Company; \$5,807,650, par value, of common stock to the unsecured creditors in satisfaction of the principal amount of their claims; \$10,000,000, par value, of common stock as a pro rata bonus with



the new first-mortgage bonds; \$14,260,570, par value, of common stock to the Western Pacific Railroad Corporation in recognition of the interest which it has as sole stockholder in the debtor.

Each of the three plans sets forth in more or less detail the proposed manner of participation of the stockholders and creditors in the plan and the method of consummation. The debtor's plan provides that it shall not be declared operative or carried out until finally approved by the Commission and confirmed by the court after acceptance by the holders of each class or classes of securities or claims affected by the plan as shall be sufficient under the provisions of section 77. The James plan provides that it shall not be carried out until it shall have been approved by the Commission and the court, pursuant to the requirements of section 77, and until it shall have been accepted by two-thirds of the creditors of each class, and by two-thirds of the stock of each class. The bondholders' committee plan provides that it shall not be carried out until it shall have been accepted by the holders of at least two-thirds in principal amount of the debtor's outstanding first-mortgage bonds, nor unless either (1) the plan shall have been accepted by creditors holding at least two-thirds in prin- [264] cipal amount of the total allowed claims of such class, and by the holders of at least two-thirds of the stock of each class, or (2) provision shall have been made for the sale of the debtor's property at public auction at a fair upset price as determined by the court, and

the payment to the nonassenting creditors of such class or the nonassenting stockholders of such class of their aliquot portion of the proceeds of the sale of such property.

None of the proposed plans is agreed to by all the parties to the proceeding.

The debtor's plan is objected to by the bondholders' committee on the grounds that it proposes an unsound capital structure in that the ratio of debt to capital stock is disproportionate, and that the total of fixed and contingent interest charges proposed is excessive in the light of the debtor's past earning experience and probable future earnings. The James plan is objected to for the same reasons. The bondholders further contend that the debtor's plan discriminates unfairly in favor of the Reconstruction Finance Corporation, and against the first-mortgage bondholders and the Railroad Credit Corporation in that it proposes to place the Reconstruction Finance Corporation on a parity with the present first-mortgage bondholders as compensation for furnishing the \$10,000,000 of new money. In proposing to give the A. C. James Company and the Railroad Credit Corporation securities on the basis of the principal amount of their notes, irrespective of the amount of their collateral security, the bondholders allege that the Railroad Credit Corporation is discriminated against. By granting all the new common stock of the reorganized company to the Western Pacific Railroad Corporation without requiring any contribution or sacrifice by that cor-

poration to or in the reorganization, the bondholders allege that undue preference is proposed.

The James plan is further protested by the bondholders' committee on the grounds that it is discriminatory in that it does not provide any fixed interest obligations for the present first-mortgage bonds; that it proposes the issue of new securities having the sole first lien upon the property of the reorganized company exclusively to the Western Pacific Railroad Corporation along with a bonus of \$150 of new common stock for each \$100 bond; proposes the waiving of all accrued interest without any compensation therefor; disregards the relative priorities of the various creditors by [265] giving the same bonus of new common stock; proposes no sinking funds for retirement of debt; makes the new bonds allotted to the present first-mortgage bondholders mature in 1987 as against a maturity in 1957 for the obligations which are proposed to be given to the so-called junior creditors; and proposes to treat the claims of the Reconstruction Finance Corporation, the Railroad Credit Corporation, and the A. C. James Company on the basis of the principal amounts of the notes rather than upon the basis of the collateral held. The bondholders' committee also objects to the James plan proposal to give the Reconstruction Finance Corporation, the Railroad Credit Corporation, and the A. C. James Company the principal amount of their notes in new 4-percent debentures, convertible into 150 percent in principal amount of 6-percent pre-

ferred stock. The bondholders' committee points out that if the debentures are converted, the new preferred stock would rank in the scale of distribution of the reorganized company's earnings substantially at the same point as the debentures; that this would result in a 9 percent annual return upon the present claims and also would operate to depress the value of the common stock of the reorganized company.

The bondholders' plan is objected to by the A. C. James Company on the grounds that it proposes an unsound and complicated capital structure, does not furnish appropriate vehicles for senior and junior financing of future capital requirements; does not preserve debt as debt; capitalizes unearned and unpaid interest as a permanent part of the capital structure; proposes excessive interest rates for certain new securities; and proposes excessive fixed charges. Certain of those objections also are advanced in regard to the debtor's plan. It is further alleged that the bondholders' plan discriminates unfairly against the other creditors and in favor of the bondholders, and does not accord sufficient recognition to the debtor's equity.

### Conclusions

By the provision of section 77(b) of the Bankruptcy Act, as amended, a plan of reorganization shall include provisions modifying or altering the rights of creditors generally, or any class of them, secured or unsecured, either through the issue of new securities of any character or otherwise; shall

provide for fixed [266] charges (including fixed interest on funded debt, interest on unfunded debt, amortization of discount on funded debt, and rent for leased railroads) in such an amount that, after due consideration of the probable prospective earnings of the property in the light of its earnings experience and all other relevant facts, there shall be adequate coverage of such fixed charges by the probable earnings available for the payment thereof; and shall provide adequate means for the execution of the plan. Subsection (e) of section 77 provides that the judge shall approve the plan certified to the court by us, if satisfied, after hearing, and without hearing if no objections are filed, that the plan complies with the provisions of subsection (b), is fair and equitable, affords due recognition to the rights of each class of creditors and stockholders, does not discriminate unfairly in favor of any class of creditors or stockholders, and will conform to the requirements of the law of the land regarding the participation of the various classes of creditors and stockholders; that the approximate amounts to be paid by the debtor, or by any corporation or corporations acquiring the debtor's assets; for expenses and fees incident to the reorganization, have been fully disclosed so far as they can be ascertained at the date of the hearing, are reasonable, are within such maximum limits as are fixed by us, and are within such maximum limits to be subject to the approval of the judge; that the plan provides for the payment of all costs of administration and all other allowances made or to be made by the judge,



except that allowances for the actual and reasonable expenses (including reasonable attorney's fees) incurred in connection with the proceedings and plan by parties, in interest and by reorganization managers and committees or other representatives of creditors and stockholders, and the actual and reasonable expenses incurred in connection with the proceedings and plan and reasonable compensation for services in connection therewith by trustees under indentures, depositaries, and such assistants as we, with the approval of the judge, may especially employ, may be paid in securities provided for in the plan if those entitled thereto will accept such payment. By the provisions of subsection (d) of section 77, the plan approved by us must meet with these requirements of subsections (b) and (e) and be compatible with the public interest, but such plan may be different from any which has been proposed. [267]

It will be observed that insofar as the capitalization of a reorganized company is concerned, section 77 contains no limitations other than that the fixed charges of the company shall be adequately covered by the probable earnings available therefor, and the plan as a whole shall be compatible with the public interest. The public interest is not defined, but it would seem obvious that to be compatible with the public interest, the plan must provide a capital structure for the reorganized company which will give it a reasonable opportunity to function efficiently and continuously as a going concern. This requires that the capitalization should not exceed

a conservative appraisal of the assets to be taken over by the reorganized company, and that proposed charges, whether fixed or contingent, be within its probable earning power.

The present reorganization of the debtor is the second since it began complete operations in 1911. A review of its financial history shows that due to an inherent lack of earning power its past operations have resulted in financial failure, and that the investment in its property has not been justified by its earnings. In *Denver & Rio Grande Investigation*, 113 I.C.C. 75, we pointed out that economically the original construction of the debtor was an ill-advised undertaking. If this reorganization is to be successful, the capital structure of the reorganized company must be realistically related to its actual earning power, and consideration given to the investment in its property only to the extent that such investment is justified by the probable earnings reasonably foreseeable for the future.

As will have been noted, January 1, 1937 is proposed as the effective date of reorganization in each of the filed plans. The obligations of the debtor, including accrued and unpaid interest, have increased considerably since that date, however, and the approval plan should provide that July 1, 1938 shall be the effective date of reorganization. Under the provisions of the debtor's plan, if modified as suggested by its counsel, the total capitalization of the reorganized company, as of that date, exclusive of no-par-value stock, would be \$94,258,367. Treating the proposed no-par-value stock at \$100 per

share, the total capitalization would be \$124,258,367. Fixed interest charges would be \$905,321, contingent interest charges \$1,993,620 (assuming interest at 4 percent on proposed collateral income notes), and total fixed and contin- [268] gent interest, together with capital and sinking funds requirements, would be \$3,695,391 per annum.

Under the bondholders' plan, computed as of July 1, 1938, the total capitalization, excluding no-par-value stock, would be \$74,270,738. Treating the proposed no-par-value stock at \$100 per share, the total minimum capitalization would be \$108,270,238, and the maximum \$123,270,238. Fixed interest would be \$905,322, contingent interest would be \$985,802, and total fixed and contingent interest, plus capital and sinking funds requirements, would be \$2,489,704 per annum.

Under the James plan, computed as of July 1, 1938, the total capitalization would be \$116,665,459. Fixed interest would be \$511,001, contingent interest \$2,387,940, and total fixed and contingent interest would be \$2,898,941 per annum. It will be noted that this plan does not provide for any capital fund or sinking fund.

The fixed interest charges proposed in each of these plans are substantially lower than the debtor's present fixed charges. From data hereinbefore set out it is apparent that the reported consolidated income of the debtor's system available for interest would have been insufficient to have met the fixed charges proposed under the James plan in 1931 and

1932, and under the debtor's and bondholders' plan in 1931, 1932, and 1933. During the 5-year period 1931-35 the debtor's average reported consolidated income available for interest was \$525,967, and if adjusted as hereinbefore suggested, it would be much less. While the earnings of the debtor showed improvement in 1936 and 1937 over those for the period 1931-35, inclusive, being \$1,902,033 in 1936 and \$1,069,785 in 1937, after eliminating extraordinary expenditures for rehabilitation and amortization for discount of funded debt, and assuming that reported expenditures for maintenance were sufficient normally to maintain the property, the decline in earnings in 1937 from 1936, and the lack of any earnings in the first six months of 1938, there having been a deficit of \$1,120,403 in those months, show conclusively, if these data are not to be ignored, that the fixed interest charges of the reorganized company should not initially and substantially exceed \$500,000, if the reorganized company is to maintain its property properly and secure necessary new capital in the future. In this latter connection, it is essential that provision be made to raise \$10,000,000 of new money for the purpose of retiring outstanding trustees' certificates. [269]

Interest at 4 percent on \$10,000,000 of new bonds would be \$400,000, and, including charges of \$111,001 on present equipment obligations of the debtor and its trustees which are to be assumed by the reorganized company, the reorganized company would be immediately faced with fixed interest charges of \$511,001 per year. We conclude, there-

fore, after a consideration of the debtor's past, present, and probable future earnings, that the plan of reorganization should provide for the immediate issue and sale of not to exceed \$10,000,000 of new first-mortgage bonds, the proceeds of which should be used to retire outstanding trustees' certificates. In the event the new bonds are not salable at par, it may be necessary for the reorganized company to obtain a loan of \$10,000,000 from the Reconstruction Finance Corporation. The approved plan should provide, therefore, that if no commitment for the purchase of such bonds is deposited with us within 60 days after approval of the plan by the court, the \$10,000,000 of bonds authorized to be issued, together with such additional bonds as may be required by us and the Reconstruction Finance Corporation in proceedings under section 5 of the Reconstruction Finance Corporation Act, shall be deposited as security for a loan of \$10,000,000 to the reorganized company. The purchase of any of the bonds by the Reconstruction Finance Corporation, or any loan by that corporation upon such bonds as collateral, will be subject to our approval under the provisions of the Reconstruction Finance Corporation Act. In view of the present unsatisfactory earnings of the debtor, and in order to provide against financial embarrassment should conditions not improve, the payment of interest on such bonds should be made only at such time as earnings are available therefor for a period of five years from the effective date of reorganization.



These bonds should be secured by a new first mortgage which should be a first lien upon all property, real and personal, and equipment, now subject to existing mortgages of the debtor or at any time acquired by the reorganized company, subject, however, to the lien of obligations issued for equipment purchased or outstanding on equipment acquired in the reorganization. To facilitate future capital financing, the total authorized issue of bonds thereunder should be limited to \$50,000,000, of which \$10,000,000, and such additional amount as may be necessary, should be sold or [270] pledged to provide the new money required in the reorganization, and the remainder should be available for issue, with our approval, to provide for expenditures for additions, betterments, improvements or extensions made after the effective date of the reorganization, in a principal amount not exceeding 75 percent of the actual cost of such additions, betterments, improvements, or extensions. The bonds should be dated as of the effective date of reorganization, should mature in 50 years, and should bear interest at the rate of 4 percent per annum, payable semi-annually. It should be provided, however, that interest accruing for a period not exceeding five years from the effective date of reorganization, or any portion thereof, on such bonds should accumulate, if not currently earned, and the payment thereof should be made only at such time as earnings are available therefor, but interest on such bonds accruing subsequent to a period not exceeding five years from the effective date of reorganization

should be a fixed charge. The bonds should be redeemable in whole or in part on any interest payment date upon 30 days' notice, at not to exceed 105 and accrued interest.

Suggestions have been made by parties to this proceeding that the authorized issue of the new bonds should not materially exceed those to be issued immediately or that restrictions against the issuance of additional bonds, when there is insufficient earnings coverage, should be provided. The latter restriction is not an unusual one; and while it may at times prove embarrassing to the reorganized company in the future, we find that the mortgage indenture of the new first-mortgage bonds should provide that new bonds in excess of the \$10,000,000 to be immediately issued for sale, or such additional amount as may be necessary for pledge in order to secure a loan of \$10,000,000, should not be issued on the basis of additional property of any kind or additions and betterments, unless the income of the reorganized company available for fixed charges in a period of 12 consecutive calendar months within the 18 calendar months immediately preceding the date of authentication and delivery of the bonds equals or exceeds 1.5 times the fixed charges, including interest on the bonds then applied for.

Considering the limited amount of fixed interest bonds approved herein, there would seem to be no real reason for the creation and maintenance of the so-called contingency reserve fund of [271] \$500,000 to be available for the payment of interest on the new first-mortgage bonds as proposed in the debt-

or's plan and the bondholders' original plan. We find, therefore, that no provision should be made for such a fund.

Since new first-mortgage bonds would not be issued in principal amount to exceed 75 percent of future capital expenditures, the balance of such expenditures must be financed through the issue of junior securities or from earnings. Under both the debtor's plan and the bondholder's plan, funds for routine expenditures for additions and betterments would be secured from the hereinbefore described capital fund contemplated under their plans. The A. C. James Company opposes the creation of such a fund, as well as sinking funds for the redemption of bonds, contending that such funds are not in accordance with the principle of sound financing, and that the Revenue Act of 1936 imposed too great a penalty on the retention of earnings for such purposes. However, the reorganized company, like other railroad companies, must secure funds for future capital expenditures. To avoid embarrassment in the securing of funds, especially for future routine additions and betterments, which are estimated by the debtor at \$500,000 annually, we find that the plan should provide for the creation of a capital fund out of the available net income remaining after payment of fixed charges. To prevent too heavy a sacrifice by present security holders, payments into the fund should not exceed \$500,000 in any one year, nor, in any event, should the total fund exceed \$1,000,000 at any time. Annual payments into the fund should be \$500,000 or such lesser

sum as may be required together with unappropriated accumulations in the fund as of the close of the calendar year prior to that for which the payment is to be computed, less charges for additions and betterments during the latter year, to bring the total in the fund to \$1,000,000. Capital expenditures reimbursed out of the capital fund should not be capitalized through the issue of additional fixed or contingent interest-bearing bonds.

The debtor proposes that sinking funds be provided for all bonds, and the bondholders propose that they apply to income bonds only. The debtor also proposes that payments into sinking funds should not be made until payment of all interest charges and payments to the capital fund have been made. The bondholders originally proposed that payment into both funds should not be made until after [272] payment of dividends on the preferred stock. The latter proposal is not now urged. In view of the relatively small issue of fixed interest bonds which we have herein found should be issuable immediately, we do not believe that provision for their retirement through a sinking fund is required. We are of the opinion, however, that provision should be made for the creation of a sinking fund for the retirement of such bonds when and if \$20,000,000, principal amount thereof, shall have been issued. Immediate provision should be made for the retirement of income bonds hereinafter approved under the plan. We find, therefore, that the plan should provide for the immediate creation, out of available net income remaining after the pay-

ment into the capital fund and interest on income bonds, of a cumulative sinking fund, in an amount up to, but not exceeding, in respect to any calendar year, one-half of 1 percent of the total principal amount of income bonds hereinafter approved for issue in the reorganization. This sinking fund should be applied to the purchase of income bonds at not exceeding their redemption price, and whenever the amount in the sinking fund exceeds \$50,000 and income bonds are not tendered or can not otherwise be purchased at less than their redemption price, the funds then in the sinking fund should be applied to the redemption of income bonds on the next succeeding interest payment date. Bonds purchased or redeemed out of the sinking fund should not thereafter be reissued.

As hereinbefore stated, the debtor's plan, modified as suggested by counsel, contemplates the issue of \$39,432,100 of 4-percent income bonds. Under the bondholders' plan, \$19,716,040 of 5-percent income bonds should be issued, and under the James plan, \$49,290,100 of 4-percent income bonds would be issued. Including the interest on fixed debt, and the requirements of the capital and sinking funds herein approved, the charges of the reorganized company under the debtor's proposal would be \$2,785,445, under the bondholders' proposal \$2,095,383, and under the James proposal, \$3,229,055. In order that any income bonds issued in the reorganization and remaining outstanding at maturity should be easily refundable, their interest charges should be well within the apparent earning power of the company



under reasonably favorable business conditions. Forecasts of higher earnings than those of the present and recent past may be supported by the record, and the annual [273] earnings of the debtor may not again descend to the lows reached in the depression, but the total of the fixed and contingent charges of the reorganized company should be limited by a consideration of the actual experience of the debtor rather than future possibilities if financial embarrassment is to be avoided. The record shows that the last year in which the debtor's unadjusted system earnings were sufficient to pay such charges as would accrue under the debtor's proposal was in 1928, under the bondholders' proposal was in 1929, and under the James proposal was in 1926. The average earnings forecast by the debtor for the period 1936 to 1940, inclusive, would be insufficient to meet the charges proposed by the debtor and the A. C. James Company. Even though interest is made dependent on earnings, the principal of any income bonds issued is debt and must be met at maturity. On the basis of the facts heretofore recited with respect to traffic and earnings, we find that the total annual fixed and contingent interest charges of the reorganized company, plus requirements for the capital and sinking funds should not exceed \$2,000,000 per annum. With fixed charges and the requirements of the capital fund herein approved amounting to \$1,011,001, interest charges and sinking fund requirements on new income bonds should be less than \$989,000, these two sums equaling \$2,000,001.

The bondholders urge that the rate of interest on the new income bonds should be 5 percent. With limited income, it is axiomatic that the higher the rate of interest the smaller the principal of bonds that may be issued. In order to allot as large an amount of new bonds as possible to present creditors, we find that the new income bonds should bear interest at the rate of 4 percent per annum. We further find that the principal amount of such bonds should not exceed \$19,716,040. Interest at 4 percent thereon would be \$788,642, and including annual requirements for a sinking fund of one-half of 1 percent for such bonds, the total of the fixed and contingent charges herein approved would amount to \$1,898,223.

The bondholders also urge that contingent interest on the income bonds be made cumulative for three years, maintaining that though low earnings might be more than offset in a subsequent period by high earnings, the benefit of those high earnings, without such accumulation, could not recoup the losses of income bondholders but would inure progressively downward to the lower classes of securi- [274] ties. In our opinion such provision for accumulation of contingent interest is fair.

The plan should provide that the new income bonds be secured by a mortgage constituting a lien, subject only to the lien of the first mortgage, upon all property from time to time subject to the lien of the first mortgage. The total authorized issue of bonds thereunder should be limited to approxi-

mately \$19,716,040. The bonds should be dated as of the effective date of the reorganization and mature in 75 years, bear interest at the rate of 4 percent per annum, payable annually, only out of the available net income of the reorganized company, and such interest should be cumulative whether earned or not, up to a maximum of 12 percent at any time. Provision should be made, however, that such interest shall not be cumulative if and as long as any deficit exists in the payment of interest on the first-mortgage bonds herein approved. The bonds should be redeemable on any interest payment date at their principal amount, plus any interest payable thereon on such interest payment date. They should be entitled to the benefit of a one-half of 1 percent sinking fund, payable out of available net income remaining after the payment of all prior charges herein approved.

The debtor's plan, if modified as suggested by counsel, and adjusted to June 30, 1938, would also provide for the issue of \$10,408,410<sup>0</sup> of collateral notes to mature in 15 years, secured by \$18,999,500 of prior lien 4-percent preferred stock. No definite rate of interest for the notes is suggested. The James plan, also adjusted, would provide for the issue of \$10,408,410 of convertible 4-percent debentures to mature in 60 years. The proposed note issue, unless provisions were made for its extension, would, of course, impose on the reorganized company the burden of the payment of the principal amount of the notes in 15 years, that is, prior to

the maturity of the new first-mortgage and income bonds. On the other hand, the collateral consisting of stock would be junior to the obligation which it secured, and thus would be of doubtful value. We can not approve this proposal, nor the James proposal, for the reasons hereinbefore stated with respect to the limitation of interest charges which may be incurred by the reorganized company.

Issues of capital stock in varying amounts are contemplated under the debtor's, the bondholders', and the James plans. The [275] amounts and the character of the stock proposed were undoubtedly influenced by the debtor's existing obligations and by the amount of debt proposed for the reorganized company under the various plans. If these plans were adjusted by providing for the issue of stock for the difference between the debt herein approved and the total capitalization (treating no-par-value stock at \$100 per share), proposed under each of them, the debtor's plan would provide for the issue of \$91,476,210 of stock, the bondholders' plan a minimum of \$75,488,081, and a maximum of \$90,488,081 of stock, and the James plan \$83,883,302 of stock. In order to meet the prior charges herein approved and to pay dividends at the rate of 5 percent on \$91,476,210 of stock, the reorganized company's income available for interest would have to be \$6,472,034; on \$75,488,081 an amount of \$5,672,627; on \$90,488,081 an amount of \$6,422,627; and on \$83,883,302 an amount of \$6,092,388.

As hereinbefore stated, the debtor's estimate of income available for interest averaged \$2,715,306 per year for the period 1936-40, inclusive, the maximum amount for any one year in the period (1940) being \$3,769,836. That amount, with prior charges of \$1,898,223, would permit the payment of dividends at the rate of 5 percent on only \$37,432,000 of stock. It is obvious, therefore, that based on the most optimistic estimate of earnings of record, the capitalization of the reorganized company must be maintained within strict limits if any material return on its capital stock is to be expected and the shares of its stock are not to become mere tokens for stock market speculation. It is true that considered alone, the data pertaining to the rate-making value of the debtor's property, and its investment, would support capitalizations approximating those proposed in the three plans. We have hereinbefore stated, however; the reasons why, in our opinion, those factors can not be of controlling importance in a determination of the capital structure for the reorganized company. Considering all relevant data of record, we find that the approved plan should provide for the immediate issue by the reorganized company of not to exceed 295,740-3/10 shares of preferred stock of the par value of \$100 per share, and not more than 313,703 shares of no-par-value common stock.

The new preferred stock, which should be authorized in the total amount of 500,000 shares, should be entitled to receive dividends at [276] the rate of 5 percent per annum in respect to each cal-



✓  
endar year before any dividends should be paid or declared upon the common stock. Such dividends should be cumulative to the extent earned in respect to any income period, but not paid; but such dividends should otherwise be non-cumulative. In event of liquidation the new preferred stock should be entitled to receive out of the assets of the reorganized company its par value plus accumulated unpaid dividends before any distribution is made to any new common stock, but should not be entitled to any further participation in such assets. The new preferred stock should be redeemable, in whole or in part, at any time at its par value plus accrued and unpaid cumulative dividends.

The plan should provide that the reorganized company shall not, without the vote or consent of the holders of at least two-thirds in par value of outstanding new preferred stock, (1) create or permit to be created any mortgage or other lien upon any of its properties, excepting the new first mortgage and new income mortgage or purchase money liens (including equipment obligations) upon property hereafter acquired, given for not more than 75 percent of the purchase price of such property; (2) create or issue any bonds, notes, or other evidences of indebtedness maturing more than two years from their date, except purchase money obligations, given for not more than 75 percent of the purchase price of property hereafter acquired; (3) create any stock, other than that authorized herein, ranking either as to assets or dividends, in priority to or on a parity with the new preferred stock; or

(4) permit any subsidiary, substantially all of whose stock shall be owned by the reorganized company, to create any mortgage or other lien upon any of the properties of the subsidiaries or issue any such bonds, notes, or other evidences of indebtedness (except purchase money liens or obligations as aforesaid), or issue any additional stock of any class, unless the obligations secured by such mortgage or other lien or such other obligations or such stock shall first be offered for acquisition by the reorganized company. Each share of the new preferred stock should have equal voting rights and privileges with any new common stock.

The total authorization of common stock should be 500,000 shares, without par value, of which about 313,703 shares may be issued forthwith. [277]

Upon the issue of the securities above approved, and assuming the sale of the new bonds, the total capitalization, excluding 313,703 shares of no-par-value common stock, would be \$62,356,217, consisting of \$3,066,117 of equipment obligations, \$10,000,000 of first-mortgage 4-percent bonds, \$19,716,040 of income mortgage 4-percent bonds, and \$29,574,060 of 5-percent preferred stock. Treating the no-par-value common stock at \$100 per share, the total capitalization would be \$93,726,517. Total fixed interest charges would be \$511,001, total fixed and contingent interest charges, plus the payments into the capital fund and sinking fund, would be \$1,898,223, and preferred dividends would be \$1,478,703, a grand total of \$3,376,926 per annum.

The available net income of the new company should be determined for the six-months' period ending December 31, 1938, and thereafter for each calendar year ending December 31 (hereinafter called income period, except that the six-month period ending December 31, 1938, also should be considered an income period) ~~as promptly as possible~~ after the termination thereof. The available net income for each income period should be determined by deducting from the consolidated income of the reorganized company and its subsidiaries available for fixed charges for such income period (determined in accordance with this Commission's accounting rules) all fixed charges of the reorganized company and its subsidiaries accrued during such income period, together with an amount representing any deficit in fixed charges, including any deficit in interest payments on the reorganized company's first-mortgage bonds which may have accrued in previous periods. The plan should provide, however, (1) that in determining available net income there should not be deducted any amounts expended from the proceeds of the trustees' certificates issued for rehabilitation purposes, notwithstanding that under our accounting rules such expenditures may be chargeable to operating expenses; and (2) notwithstanding that the reorganized company should not have come into ownership and possession of the properties now operated by the trustees of the debtor on or before July 1, 1938, available net income for any period after July 1, 1938, until the

reorganized company comes into possession and operation of such properties, should be computed as if the reorganized company had come into such ownership or possession on July 1, 1938, and had issued, as [278] of that date, the new securities issuable under the plan, other than the \$10,000,000 of new first-mortgage bonds, and in lieu of interest on such bonds there should be charged the amount of interest actually accruing during such period upon any trustees' certificates or other obligations issued to provide funds for the rehabilitation program.

All three plans before us are predicated on the priority of the existing first mortgage over the general mortgage, and all parties admit that the first mortgage is a first lien on the main line of the debtor's railroad and the securities physically pledged under that mortgage. The trustee under the first mortgage and the holders of bonds issued under that mortgage contend that the first mortgage is a first lien on substantially all the debtor's property, except equipment subject to existing leases, conditional-sale agreements, or equipment-trust agreements. The general mortgage trustee and those creditors with whom general-mortgage bonds are pledged contend, however, that the first mortgage is not a lien, or is a lien only to the extent of the proceeds of first-mortgaged bonds expended thereon, on cash and collateral held by the trustees under the general mortgage, on the Northern California extension, on the debtor's equity in rolling stock subject to leases, conditional sale agreements,

or equipment trust agreements, and on property, in general, purchased either in whole or in part from free funds. Those parties contend further that most of the property just described is not only free from the lien of the first mortgage but is subject to the lien of the general mortgage, and that its value is sufficient for the full payment of all the debts secured under the general mortgage, with interest. With the exception of the A. C. James Company, they assert that the first-mortgage bondholders are not entitled to preferential treatment.

While final adjudication of this and similar questions must be made by the court, it becomes our duty, in the absence of such adjudications, to determine them preliminarily for the purposes of **consideration of the plans before us.**

Since most of the property which is in dispute was acquired after the date of the first mortgage, the primary question involved is whether such property is covered by the after-acquired clause contained in the granting clauses of the first mortgage.

[279]

Clause first of the granting clauses covers in detail and by a general statement all property which had been owned by the debtor's predecessor, except only cash items. Granting clause third covers "any and all property and facilities of any and every kind and description \* \* \* which may from time to time hereafter be acquired or constructed by or belong to" the debtor, if such after-acquired property falls within one of the four following categories:



(1) If any "First mortgage bonds or proceeds thereof or cash deposited" under the first mortgage have been authenticated or paid out "on account of the purchase, acquisition or construction thereof or work therein"; or

(2) If the property constitutes "an integral part or parts of lines of railroad, extensions, branches or other property subject to the lien" of the first mortgage; or

(3) If the property is "used or acquired for use in or for the maintenance or operation of or pertaining to" any of the property subject to the lien of the first mortgage; or

(4) If the property consists of shares of stock or of other securities of the Salt Lake City Union Depot & Railroad Company or Standard Realty & Development Company, or any subsidiary as defined.

Granting clause fifth covers almost every kind of property and facility used or useful in the operation of a railroad (including additional tracks, spurs, equipment, material and supplies, and land), ending with the generality "all other property of every description and all rights and interests in or with respect to the use of property \* \* \* whether now owned \* \* \* or at any time hereafter acquired", if "appurtenant to or used or held for use as, or as a part of or as parts of, or to facilitate or safeguard the maintenance or operation of, any lines of railroad, extensions, branches \* \* \* or other prop-

erties now or at any time hereafter subject to the lien" of the first mortgage.

Following granting clause sixth is a proviso permitting the debtor by the use of free funds to acquire property free of the lien of the first mortgage if such property is not of the character described in the four subdivisions of granting clause third.

[280]

The Northern California extension, various branches and spurs, and equipment used under leases, contracts, or equipment-trust agreements, are the principal items of property in dispute. With respect to the first two classes of property we are satisfied from the record that substantial amounts of the proceeds of first-mortgage bonds were used in their acquisition or construction, or at least "on account of the purchase, acquisition or construction thereof or work thereon". We construe the latter language to mean that the lien of the first mortgage attaches to after-acquired extensions if the purchase, acquisition, or construction thereof, or any work thereon, be financed in any part with first-mortgage bonds or cash deposited under that mortgage.

While the construction of the Northern California extension was financed in part with the proceeds of certain debentures which were subsequently exchanged for general and refunding bonds, it is not contended that the debentures were secured by a lien on the extension. Moreover, the record is clear that there was no intent to create a purchase money

lien on the extension in favor of the debentures. The same is true with respect to the advances from the Reconstruction Finance Corporation.

We conclude that, for the purpose of determining the equity of plans of reorganization for the debtor, the lien of the general mortgage on the Northern California extension and various branches and spurs in question should be considered subject to the lien of the first mortgage.

The debtor's equity in rolling stock subject to leases, conditional-sale agreements, or equipment-trust agreements, would seem to be covered by the after-acquired property clause in the third paragraph, as well as by the fifth paragraph, of the granting clauses unless the proviso at the end of the granting clauses negatives such a construction. The proviso reads as follows:

\* \* \* ; and the company may, unless First Mortgage Bonds shall have been authenticated and delivered or their proceeds or other cash deposited hereunder paid out against the same, purchase and acquire equipment free from the lien hereof, by lease, conditional sale agreement or under any form of equipment trust, or purchase such equipment and issue obligations therefor secured by mortgage or pledge of such equipment superior to the lien of this indenture. [281]

The latter provision, however, should be construed both in the light of the language which precedes it in the same paragraph and in the light of the paragraph which follows the habendum clause. The latter paragraph reads as follows:

Subject, however, as to all equipment now owned to the equipment trust or conditional sale agreements secured thereon, and to equipment hereafter acquired, to the equipment trust or conditional sale agreements to which the same shall be subject as permitted hereby \* \* \*

If all equipment acquired under equipment trusts was to be entirely free of the lien of the first mortgage, it is not apparent why the words "equipment trust or conditional sale agreements to which the same shall be subject as permitted hereby" were made part of the last quoted provision. We consider, for the purposes of a plan of reorganization, that since the equipment in question was acquired for use, and was actually used, on the mortgaged lines, the debtor's equity in that equipment is subject to the lien of the first mortgage.

We consider that the property characterized as non-carrier real estate is also covered by the lien of the first mortgage. This property was owned by the predecessor of the debtor, and the general and refunding trustee contends that it did not become subject to the lien of the first mortgage because the reorganization plan, pursuant to which the present first-mortgage bonds were issued, contemplated that

such bonds should constitute a lien upon only railway properties. No such distinction as urged by the general-mortgage trustee appears in the language of the mortgage itself, and it is not clear that the use of the words "railway properties" in the previous plan of reorganization was intended to relate only to property used in carrier service.

With the exception of the notes of the Deep Creek Railroad Company and the Standard Realty & Development Company, there is no contention that the cash and collateral held by the trustee under the general and refunding mortgage are not free from the lien of the first mortgage. While due recognition must be accorded to the rights of the creditors with whom are pledged general-mortgage bonds, those creditors are not entitled to the same treatment as first-mortgage bondholders, who should be considered as having a first lien upon practically all the assets of the debtor. It follows [282] that holders of the debtor's first-mortgage bonds should receive securities of a higher rank than those allotted to other creditors, at least to the extent that existing conditions will permit.

Since the notes held by the Reconstruction Finance Corporation, Railroad Credit Corporation, and A. C. James Company are secured by the pledge of the debtor's general-mortgage bonds, they clearly are entitled to priority over the unsecured claims of the Western Pacific Railroad Corporation and the Western Realty Company. In turn, the claims of



the latter are entitled to priority over the existing stockholders.

According to the trustees' balance sheet of June 30, 1938, existing first-mortgage bonds were outstanding in the principal amount of \$49,290,100 and accrued and unpaid interest thereon amounted to \$11,914,521, a total of \$61,204,621; the indebtedness of the debtor to the Reconstruction Finance Corporation, Railroad Credit Corporation, and A. C. James Company, including accrued and unpaid interest, totaled \$12,317,842; the indebtedness of the debtor to the Western Pacific Railroad Corporation, including accrued and unpaid interest, was \$7,609,370; the debtor's indebtedness to the Western Realty Company, including accrued and unpaid interest, was \$60,417; a grand total of \$81,192,250. Under the capital structure herein approved, there will be available for distribution to these creditors in the order of their priority \$19,716,040 of new income mortgage bonds, \$29,574,060 of new preferred stock, and 313,703 shares of no-par-value common stock. Treating the no-par-value common stock at \$100 per share, a total par value of \$80,660,400 of securities will thus be available for distribution. Obviously, if the creditors' claims are to be accorded priority over the stockholders, there will remain no securities available for distribution to stockholders under the capital structure herein approved.

Under the provisions of section 77 stockholders are not entitled to participate in the plan if we find

and the judge affirms the finding, that at the time of the finding the equity of such stockholders has no value. Section 77 also contains a similar provision with respect to creditors whose claims have been found to have no value. We have hereinbefore found that considering the past, present, and probable future earnings of the debtor, its investment, the data of record pertaining to its rate-making value; and all other relevant data of record, we can not approve the issue of [283] new securities in a greater amount than that hereinbefore approved. On the same basis and for the same reasons we find, therefore, that there is no equity over and above the securities hereinbefore approved; that the equity of the existing stock has no value, and hence holders of such stock are not entitled to participate in the plan. Further, considering that the reorganized company's income available for interest and dividends must total \$4,318,035, plus any undistributed profits tax that will be payable, before dividends of \$3 per share may be paid on the new common stock, it is clear that even though all the securities remaining available for distribution after satisfying the claims of the first-mortgage bondholders are allotted to the other secured creditors, such securities will be inadequate in value to satisfy their claims. For this reason, and for the reasons stated with respect to the finding that the equity of the existing stock has no value, we find that the claims of the unsecured creditors, of the Western Pacific Railroad Corporation, and of the Western Realty Company,

have no value, and hence no securities or cash should be distributed under the plan in respect to those claims.

Proceeding to the allocation of the available securities, the plan should provide that all of the new income bonds, \$19,716,040, principal amount, all of the new preferred stock, \$29,574,060, par value, and 154,241 shares of the new no-par-value common stock, should be allotted to the holders of existing first-mortgage bonds. The remaining 159,462 shares of the no-par-value common should be allotted to the secured noteholders on the basis indicated below. The holders of the first-mortgage bonds (with March 1, 1934, and subsequent coupons) should receive for each \$1,000, principal amount, of such bonds and accrued and unpaid interest thereon approximately (a) \$400 of new income 4-percent bonds, (b) \$600 of new 5-percent preferred stock, and (c) 3.13 shares of new no-par-value common stock.

While each of the notes held by the A. C. James & Company, Reconstruction Finance Corporation, and Railroad Credit Corporation is secured by the pledge of the debtor's general and refunding bonds, the bonds pledged thereunder are of varying amounts. Thus, the debtor's total indebtedness to the Reconstruction Finance Corporation, according to the trustees' balance sheet, is \$3,612,181, although that corporation holds as pledgee 56.6 per- [284] cent of that amount of such bonds. The debtor's indebtedness to the Railroad Credit Corporation

amounts to \$2,580,906, and 21.1 percent of that amount is represented by the bonds pledged. The total indebtedness to the A. C. James Company amounts to \$6,124,755, and 22.3 percent of that amount is represented by bonds pledged. Having found that 159,462 shares of common stock available for distribution are inadequate in value to satisfy the aggregate claims of these parties, it follows that it would be inequitable to distribute such stock in the proportion that each claim bears to the total amount of such stock. The value of each of the claims is proportionate to the collateral securing it, and we find that the allotment of the stock should be made on the basis of the collateral held rather than on the amount of the claims. This would result in the Reconstruction Finance Corporation receiving 90,255½ shares, the Railroad Credit Corporation 33,646½ shares, and the A. C. James Company 35,560 shares of common stock.

The plan should provide, however, that its approval and confirmation in no wise disturbs or alters the rights of the Reconstruction Finance Corporation and the Railroad Credit Corporation in collateral pledged with them by parties other than the debtor.

The plan should further provide that subscription warrants, entitling the holders thereof to purchase the new first-mortgage bonds at par not later than 45 days after the confirmation of the plan, should be issued to the Reconstruction Finance Corporation, Railroad Credit Corporation, and A. C.

James Company, in proportion to the amounts of general-mortgage bonds now held by them respectively. If any of these creditors should fail to subscribe for its full proportion, the other or others of such creditors should be permitted to subscribe for such unsubscribed balance, in the proportion which the existing general-mortgage bonds held by them, respectively, bear to the total amount of general-mortgage bonds held by those electing to subscribe for their full proportion. Should the Reconstruction Finance Corporation, Railroad Credit Corporation, and A. C. James Company fail to subscribe for the new bonds in accordance with the above terms, holders of first-mortgage bonds should be entitled to subscribe for them upon the same terms and conditions as those parties within a period of 60 [285] days after confirmation of the plan, and the contingent rights of subscription granted to the first-mortgage bondholders should be evidenced by appropriate warrants. Holders of warrants should be required to elect prior to the expiration of the warrants, in each case, the extent to which they will exercise their subscription rights.

Under both the debtor's plan and the bondholders' committee plan current liabilities of the debtor incurred in the ordinary conduct of its business prior to the institution of this proceeding, current liabilities and obligations of the debtor and of its trustees incurred during this proceeding, and all other claims, liabilities, or obligations for which specific provision is not made in those plans, are



not to be affected by the plans, but to the extent that such claims, liabilities, or obligations are not paid by the debtor or its trustees pursuant to order of the court, they are to be paid in cash or assumed by the reorganized company. According to the record, current liabilities incurred in the ordinary conduct of the debtor's business prior to this proceeding were of a nominal amount. We approve such provisions.

Each of the three plans before us propose different conditions under which the plan shall be consummated. The James plan affirmatively provides that it shall not be consummated until accepted by two-thirds of each class of creditors and two-thirds in amount of each class of stock. Reorganizations under section 77 are primarily premised upon the acceptance of plans by two-thirds or more of each class of creditors and stockholders voting thereon. Congress recognized, however, that the public interest might, under certain conditions, require the confirmation of a plan of reorganization even though it were not accepted by all classes of creditors and stockholders, and provisions of this effect are included in section 77. To approve a provision in a plan of reorganization by which a minority of a class of creditors or stockholders effectively could block the reorganization, although the plan conformed to the requirements of the statute in all respects would, in our opinion, give such a minority a right not contemplated by the law, and,

also, would be contrary to the intent, if not the letter, thereof.

The provision in the bondholders' committee plan to the effect that its plan shall not be confirmed until at least two-thirds of the [286] holders of the debtor's first-mortgage bonds accepted it, would seem to be objectionable for the same reason as that applying to the provision in the James plan. The bondholders' proposal that the plan provide for the sale of the debtor's property at an upset price as determined by the court in the event the holders of more than one-third in principal amount of any class of creditors, or the holders of more than one-third of the shares of stock of any class, shall not have accepted the plan, after the holders of at least two-thirds in principal amount of the existing first-mortgage bonds shall have accepted the plan, is, in our opinion, an unnecessary and objectionable provision, at least insofar as the instant proceeding is concerned. Section 77(e) provides that the submission of the plan to any class of stockholders and any class of creditors shall not be necessary if we have found, and the judge shall have affirmed the finding, that the equity of such class of stockholders and the interests of such class of creditors have no value. Under our previous findings herein, and if the judge approves the plan, it will be necessary to submit the plan only to the holders of the debtor's first mortgage bonds and to the holders of its secured notes. To require the submission of the plan to unsecured creditors and to stockholders, as would

be necessary under the bondholders' proposal, would be the requiring of an act not called for by the statute, if not contrary thereto, and unnecessary for the execution of the plan. Considering the first mortgage bondholders and the secured creditors alone, the effect of the proposal would be possibly, if not probably, to influence the secured note holders to accept the plan even though such holders would not voluntarily accept the plan were it not for such a provision. We see no necessity for the possible coercion of the secured note holders to accept the plan, and, therefore, do not approve the proposal. The plan should provide that it shall be accepted and confirmed, or confirmed without acceptance, in accordance with the provisions of section 77.

Both the bondholders' plan and the James plan contemplate the formation of a reorganization committee with broad powers. No provision for such a committee is made in the debtor's plan, although it does provide that representatives of the bondholders' committee shall represent the members of that committee in the [287] reorganization, and that the form and provisions of the several indentures, bonds, stock certificates, and other instruments in connection with the reorganization shall be approved by the bondholders' committee.

We recognize that it is impracticable to specify in detail the form and provisions of the various indentures, bonds, stock certificates, and other instruments which must be executed in consummating the reorganization proceeding, although the terms and

provisions thereof are of great importance to those participating in the proceeding. For this reason the plan approved by us will provide for the formation of a committee, after approval of the plan by us and by the court, with power to determine, subject to the approval of the court, the form and provisions of the indentures, bonds, stock certificates, and other instruments, in connection with the carrying out of the plan. The committee also will have power, but only such power as necessary, to carry out the plan in accordance with its provisions subject to the direction of the court. The committee should consist of three members, one of whom should be nominated by the committee representing the first-mortgage bondholders, one by the Reconstruction Finance Corporation, Railroad Credit Corporation, and A. C. James Company, as a group, and the remaining member by purchasers of the new first-mortgage bonds to be issued to provide the new money in the reorganization, or, if no commitment be received for the purchase of such bonds, by the party or parties advancing the money for the retirement of the trustees' certificates.

Submission of the plan to the creditors for acceptance or rejection will be contingent upon the deposit with us, not more than 60 days after its approval by the court, of tentative commitments for the purchase of all the \$10,000,000 of new first-mortgage bonds to be sold under the plan, or, within 75 days after such approval, a tentative commitment on the part of the Reconstruction

Finance Corporation, to make the required loan of \$10,000,000.

Under the foregoing, the plan of reorganization would provide as follows:

1. The assumption by the reorganized company of the outstanding equipment trusts, Baldwin lease, and Pullman contract of the debtor and its trustees.

[288]

2. The immediate issue by the reorganized company of \$10,000,000, principal amount, or such additional amount as may be necessary in the event a loan of \$10,000,000 must be secured, of 50-year first-mortgage 4-percent bonds, \$19,716,040, principal amount, of 75-year income mortgage 4-percent bonds, \$29,574,060, par value, of 5-percent preferred stock, and 313,703 shares of no-par-value common stock.

3. The sale of the \$10,000,000 principal amount, of new first-mortgage bonds at par or the borrowing of \$10,000,000 through the pledge of new first-mortgage bonds.

4. The creation and maintenance of a capital fund of not to exceed \$500,000 in any one year, nor \$1,000,000 at any time, to be accumulated out of available net income.

5. The immediate creation and maintenance of a one-half of 1 percent sinking fund for the retirement of the new income bonds out of available net income remaining after payments into the capital fund, and payment of interest on the new income



bonds; and the creation out of available net income remaining after payment of fixed charges of a similar fund for the retirement of first-mortgage bonds, when and if \$20,000,000, principal amount, thereof are issued.

6. The holders of the debtor's existing first-mortgage bonds (with March 1, 1934, and subsequent coupons) to receive in exchange for each \$1,000, principal amount, of such bonds and accrued and unpaid interest thereon approximately (a) \$400 of new income 4-percent bonds, (b) \$600 of new 5-percent preferred stock, and (c) 3.13 shares of new common stock, and, subject to the terms and conditions herein provided, the contingent right to subscribe for new first-mortgage bonds to be issued to provide new money.

7. The Reconstruction Finance Corporation, Railroad Credit Corporation, and A. C. James Company, holders of the debtor's notes which are secured by the pledge of the debtor's general mortgage bonds, to receive in exchange therefor and for accrued unpaid interest thereon, 159,462 shares of new no-par-value common stock, the stock to be distributed among them on the basis herein- [289] before described, together with warrants to subscribe for the purchase of the new first-mortgage bonds.

8. The formation of a committee with such power as may be necessary to carry out the plan, and to determine, subject to the approval of the court, the form and provisions of the indentures, bonds, stock certificates, and other instruments, in

connection with the carrying out of the plan; the committee to consist of three members, one to be named by the committee representing first-mortgage bondholders, one by the Reconstruction Finance Corporation, Railroad Credit Corporation, and A. C. James Company, as a group, and the remaining member by the purchasers of the new first-mortgage bonds to be issued to provide the new money in the reorganization, or by the party or parties advancing the money necessary to retire the trustees' certificates.

9. The obligations of the debtor (other than to the Western Pacific Railroad Corporation and the Western Realty Company, unsecured claimants) not specifically herein provided for shall be paid by the debtor or the reorganized company or assumed by the reorganized company.

10. The Western Pacific Railroad Corporation and the Western Realty Company, unsecured claimants, to receive no securities or cash in satisfaction of their claims, since such claims are found to be without value.

11. The present holders of the debtor's capital stock not to participate in the plan, since the present stock of the debtor is found to be without value.

12. The plan to be accepted and carried out in accordance with its terms and the provisions of section 77 of the Bankruptcy Act, under the direction of the court.

13. The plan to be effective as of July 1, 1938.

The plan also will provide that existing mortgages on the debtor's properties be released and canceled, and all funds on deposit with the debtor's mortgage trustees representing sums paid from time to time to the trustees for the release of properties, sale of scrap, and otherwise, and all collateral pledged under the mortgages, be surrendered to the reorganized company free from existing mort- [290] gage liens, after deductions therefrom of any amounts which the court may find should be deducted under the provisions of the mortgages and consistent with the plan of reorganization herein approved. The plan should provide further that all collateral pledged by the debtor as security for its notes to the Reconstruction Finance Corporation, Railroad Credit Corporation, and A. C. James Company shall be surrendered to the reorganized debtor. The Railroad Credit Corporation also should release and surrender to the reorganized company its rights and interests in the debtor's distributive shares under the marshaling and distributing plan, 1931, from and after the effective date of the plan, and any proceeds from such shares applied by the Railroad Credit Corporation to the payment of principal and/or interest of and upon the obligations of the debtor after the effective date of the plan, unless such application shall have been made by authority of the court of competent jurisdiction, shall be turned over to the reorganized company.

In view of the provisions of section 77(b), when a plan finally is adopted, we shall give considera-

tion to the granting of such authorization for the issue of such securities as may be required and appropriate for the execution of the plan.

We find that the plan herein approved will meet with the requirements of section 77(b)(e) of the Bankruptcy Act, and will be compatible with the public interest.

The journal entries covering the necessary accounting adjustments should be submitted to us for approval before they are recorded on the books of the debtor or of the reorganized company.

An appropriate order will be issued.

---

Eastman, Commissioner, concurring in part:

I am in accord with the findings of the majority with two exceptions. For the reasons stated in my expression of partial concurrence in *Spokane International Ry. Co. Reorganization*, 228 I.C.C. 387, 408-411, I do not favor the provision for the creation and maintenance of a so-called capital fund. Nor do I favor the provision that additional first mortgage bonds "shall not be issued on the basis of additional property of any kind or additions and betterments, unless the income of the reorganized company available for [291] fixed charges in a period of 12 consecutive months within the 18 calendar months immediately preceding the date of authentication and delivery of the bonds equals or exceeds 1.5 times the fixed charges, including inter-

est on the bonds then applied for". This may be, and I think is, a very wise general rule to follow, but we have entire control of the matter under section 20a of the Interstate Commerce Act. No additional bonds can at any time be issued without our specific approval. That being so, I see no good reason for tying our own hands for the future by the incorporation in the plan of reorganization of an inflexible rule of this character. Exceptional conditions may arise making the application of such a rule unwise and contrary to the public interest in some particular instance.

Commissioner Aitchison authorizes me to state that he does not favor provision for the creation and maintenance of a capital fund in this case.

---

Miller, Commissioner, dissenting in part:

In view of the possibility of legislation at the next session of the Congress to compel consolidation of railroads into a few systems, or even into one system, which would obviate the necessity of reorganization of the railroads now in bankruptcy and also taking into consideration the fact that railroads can not be reorganized to the best advantage under present economic conditions, I am of the opinion that it would be in the interest of the security holders to defer this reorganization.

I agree with the conclusions in the report that present fixed charges must be practically eliminated



if the reorganization is now to be effectuated. I disagree in some particulars with other conclusions reached by the majority. This applies especially as to the capital fund required and the amount of capitalization allowed. The reasons for my objection to a capital fund are well stated in Commissioner Eastman's concurring-in-part expression in *Spokane International Ry. Co. Reorganization*, 228 I.C.C. 387, 408-411, in which I concurred.

In connection with capitalization the majority state (page 52, mimeograph):

- It is true that considered alone, the data pertaining to the rate-making value of the debtor's property, and its investment, [292] would support capitalizations approximating those proposed in the three plans. We have hereinbefore stated, however, the reasons why, in our opinion, those factors can not be of controlling importance in a determination of the capital structure for the reorganized company.

With this conclusion I can not agree but am strongly of the view that the capitalization should be generally on the basis of original cost less depreciation amounting to something over \$120,000,000, which is about the same as is proposed in two of the three plans referred to in the above quotation. The no-par-value common stock may have little or no market value when the company is reorganized, but the issuance in the neighborhood of \$30,000,000 more than the majority authorize would

give the present stockholders a chance to participate in the future profits of the reorganized company.

Commissioner Rogers did not participate in the disposition of this proceeding. [293]

---

### ORDER

At a General Session of the Interstate Commerce Commission, held at its office in Washington, D. C., on the 10th day of October, A. D. 1938.

---

Finance Docket No. 10913

The Western Pacific Railroad Company  
Reorganization

Investigation of the matters and things involved in this proceeding having been made, a hearing having been held, and this Commission having, on the date hereof, made and filed a report containing its findings of fact and conclusions thereon, and a full statement of the reasons for its conclusions, which report is hereby referred to and made a part hereof:

It is ordered, That the following plan of reorganization of the Western Pacific Railroad Company, debtor, be, and it is hereby, approved:

A. The effective date of said plan shall be July 1, 1938.

B. The term "reorganized company", as used herein, means the corporation in which will be vested the assets of the debtor pursuant to the plan. It may be the existing company with a modified charter, or a new corporation organized for the purpose.

C. The capitalization of the reorganized company, immediately after the consummation of the plan, shall be substantially as follows: Undisturbed equipment trusts, Baldwin lease, and Pullman contract \$3,066,117; first-mortgage 4-percent bonds \$10,000,000, or a short-term note for \$10,000,000; income mortgage 4-percent bonds \$19,716,040; 5-percent preferred stock \$29,574,060; common stock without par value 313,703 shares.

D. The first-mortgage bonds shall be secured by a mortgage constituting a first lien upon all property, real and personal, and equipment at any time acquired by the reorganized company, subject, however, to the lien of any equipment obligations issued and [294] outstanding on equipment acquired by the reorganized company in the reorganization. The total authorized issue of bonds thereunder shall be limited to \$50,000,000, of which \$10,000,000 shall be sold on terms to be approved by this Commission, to provide the new money required in the reorganization, or shall, with such additional amount of such bonds as may be necessary, be pledged under a \$10,000,000 short-term note; and the remainder shall be reserved to be issued, with our approval, to provide

for, or to reimburse the reorganized company for, expenditures for additions, betterments, improvements, or extensions made after the effective date of the reorganization, in a principal amount not exceeding 75 percent of the actual cost of such additions, betterments, improvements, or extensions. The bonds shall be dated as of the effective date of reorganization and shall mature in 50 years; shall bear interest at the rate of 4 percent per annum payable semiannually; provided, however, that interest accruing for a period not exceeding five years from the effective date of reorganization, or any portion thereof, on such bonds shall accumulate and payment thereof shall be made only at such time as earnings are available therefor; and provided further, that interest on such bonds accruing subsequent to a period not exceeding five years from the effective date of reorganization shall be a fixed charge. The bonds shall be redeemable, in whole or in part, on any interest payment date upon 30 days' notice, at not to exceed 105 and accrued interest. Bonds in excess of the \$10,000,000 to be sold, or in excess of such additional amount as may be necessary for pledge, to provide the new money required in the reorganization, shall not be issued on the basis of additional property of any kind or additions and betterments, unless the income of the reorganized company available for fixed charges in a period of 12 consecutive calendar months within the 18 calendar months immediately preceding the date of authentication and delivery of the bonds equals or

exceeds 1.5 times the fixed charges, including interest on the bonds then applied for. Whenever \$20,000,000 of such bonds shall have been issued, a one-half of 1 percent sinking fund, payable out of available net income remaining after the payment of all fixed charges, shall be created for the redemption of such bonds.

E. The ~~income-mortgage~~ bonds shall be secured by a mortgage constituting a lien, subject only to the lien of the first mortgage, [295] upon all property from time to time subject to the lien of the first mortgage. The total authorized issue of bonds thereunder shall be limited to \$19,716,040. The bonds shall be dated as of the effective date of the reorganization and shall mature in 75 years, shall bear interest at the rate of 4 percent, payable annually, and only out of available net income of the reorganized company, and such interest shall be cumulative, whether earned or not, up to a maximum of 12 percent at any time; provided, however, that no interest shall be cumulative if and as long as any deficit exists in the payment of interest on the first-mortgage bonds herein approved. The bonds shall be redeemable on any interest payment date at their principal amount, plus any interest payable thereon upon such interest payment date. They shall be entitled to the benefit of a one-half of 1 percent sinking fund, payable out of available net income remaining after the payment of all prior charges herein and hereafter approved.



F. The preferred stock shall be authorized in the total amount of 500,000 shares of the par value of \$100 per share, of which 295,740-3/5 shares shall be issued forthwith for distribution to the present first-mortgage bondholders, and shall be entitled to receive dividends at the rate of 5 percent per annum in respect to each calendar year before any dividends shall be paid, or declared, upon the common stock. Such dividends shall be cumulative to the extent earned in respect to any income period, but not paid; but such dividends shall otherwise be noncumulative. In event of liquidation the preferred stock shall be entitled to receive out of the assets of the reorganized company its par value plus accumulated unpaid dividends before any distribution is made to any common stock, but shall not be entitled to any further participation in such assets. The preferred stock shall be redeemable, in whole or in part, at any time at its par value plus accrued and unpaid cumulative dividends.

The reorganized company shall not, without the vote or consent of the holders of at least two-thirds in par value of outstanding preferred stock (1) create or permit to be created any mortgage or other lien upon any of its properties, excepting the new first mortgage and new income mortgage or purchase money liens (including equipment obligations) upon property hereafter acquired; given [296] for not more than 75 percent of the purchase price of such property; (2) create or issue any bonds, notes, or other evidence of indebtedness ma-

turing more than two years from their date, except purchase money obligations, given for not more than 75 percent of the purchase price of property hereafter acquired; (3) create any stock, other than that authorized herein, ranking, either as to assets or dividends, in priority to or on a parity with, the preferred stock; or (4) permit any subsidiary, substantially all of whose stock shall be owned by the reorganized company, to create any mortgage or other lien upon any of the properties of the subsidiaries or issue any such bonds, notes, or other evidences of indebtedness (except purchase money liens or obligations as aforesaid), or issue any additional stock of any class, unless the obligations or such stock shall first be offered for acquisition by the reorganized company. Each share of preferred stock shall have equal voting rights and privileges with any common stock issued by the reorganized company.

G. The common stock shall be authorized in a total amount of 500,000 shares, without par value, of which 313,703 shares shall be issued forthwith for distribution to the first-mortgage bondholders, Reconstruction Finance Corporation, Railroad Credit Corporation, and A. C. James Company.

H. Available net income shall be determined for the six-month period ending December 31, 1938, and thereafter for each calendar year ending December 31 (hereinafter called income period, except that the six-month period ending December 31, 1938, also shall be considered an income period), as promptly

as possible after the termination thereof. Available net income for each income period shall be determined by deducting from the consolidated income of the reorganized company and its subsidiaries available for fixed charges for such income period (determined in accordance with this Commission's accounting rules) all fixed charges of the reorganized company and its subsidiaries accrued during such income period, together with an amount representing any deficit in fixed charges including deficit in interest payments on the reorganized company's first-mortgage bonds which may have accrued in previous periods; provided, however, (1) that in determining available net income there shall not be deducted any amounts expended from the proceeds of the trustees' certificates issued for rehabilitation purposes, notwithstanding that under our accounting rules such expenditures may be chargeable to operating expenses; and (2) notwithstanding that the reorganized company shall not have come into ownership and possession of the properties now operated by the trustees of the debtor on or before July 1, 1938, available net income for any period after July 1, 1938, until the reorganized company comes into possession and operation of such properties, shall be computed as if the reorganized company had come into such ownership or possession on July 1, 1938, and had issued, as of that date, the new securities issuable under the plan, other than the \$10,000,000 of new first-mortgage bonds, and in lieu of interest on such bonds there should be charged the amount of interest actually

accruing during such period upon any trustees' certificates or other obligations issued to provide funds for the rehabilitation program.

I. Available net income for each income period shall be applied to the following purposes and in the following order:

1. To the creation, if and when \$20,000,000 of first-mortgage bonds hereinbefore approved shall have been issued, of a cumulative ~~sinking fund~~, in an amount up to, but not exceeding, in respect to any calendar year, one-half of 1 percent of the total principal amount of such bonds issued by the reorganized company. Such sinking fund shall be applied to the purchase of first-mortgage bonds at not exceeding their redemption price, and whenever the amount in the sinking fund exceeds \$50,000 and first-mortgage bonds are not tendered or can not otherwise be purchased at less than their redemption price, the fund then in the sinking fund shall be applied to the redemption of the income-mortgage bonds on the next succeeding interest payment date. Bonds purchased or redeemed out of the sinking fund shall not thereafter be reissued.

2. To the creation of a capital fund, to be applied to, or to provide for, or to reimburse the treasury of the reorganized company for capital investments (as defined by this Commission's Classification of Income Profit and Loss and General Balance Sheet Accounts for Steam Railroads, and including therein initial and principal payments upon equipment leased under equipment trusts or pur-

chased under conditional sale agreements). Annual pay- [298] ments into the fund shall be \$500,000, or such lesser sum as may be required, together with unappropriated accumulations in the fund as of the close of the calendar year prior to that for which the payment is to be computed, less charges for additions and betterments during the latter year, to bring the total in the fund to \$1,000,000; provided, however, that (a) the capital fund shall not exceed \$1,000,000 at any one time; and (b) capital expenditures reimbursed out of the capital fund shall not be capitalized through the issue of additional fixed or contingent interest-bearing bonds.

3. Any then available net income shall be applied to the payment of the contingent interest on the outstanding income-mortgage 4-percent bonds accruing during the income period ending on the next preceding December 31, and, to the extent unpaid, any accumulations thereof.

4. Any then remaining available net income shall be applied to the creation of a cumulative sinking fund, in an amount up to, but not exceeding, in respect to any calendar year, one-half of 1 percent of the total principal amount of income-mortgage bonds issued in the reorganization. Such sinking fund shall be applied to the purchase of income-mortgage bonds at not exceeding their redemption price, and whenever the amount in the sinking fund exceeds \$50,000 and income-mortgage bonds are not tendered or can not otherwise be purchased at less than their redemption price, the funds then in the sinking fund shall be applied to the redemption of



the income-mortgage bonds on the next succeeding interest payment date. Bonds purchased or redeemed out of the sinking fund shall not thereafter be issued.

5. Any then remaining available net income shall be applied if, and to the extent that, such dividends shall be declared by the board of directors of the reorganized company, to the payment of dividends at the rate of 5 percent per annum upon the preferred stock in respect to the income period ending on the next preceding December 31.

6. Any then remaining available net income may be applied to any proper corporate purpose of the reorganized company, including dividends on the common stock. [299]

J. The existing securities of the debtor and its trustees shall be treated as follows:

(1) Outstanding existing equipment trusts, Baldwin lease, and Pullman contract of the debtor and its trustees shall remain undisturbed and shall be assumed by the reorganized company.

(2) Holders of existing first-mortgage bonds (with March 1, 1934, and subsequent coupons) shall receive for each \$1,000 principal amount of such bonds and accrued and unpaid interest thereon approximately (a) \$400 of new income-mortgage 4-percent bonds, (b) \$600 of new 5-percent preferred stock, (c) 3.13 shares of new common stock, and (d) subject to the terms and conditions hereinafter provided, the contingent right to subscribe for new first-mortgage bonds to be issued to provide new money.

(3) Notes to the Reconstruction Finance Corporation, Railroad Credit Corporation, and A. C. James Company, together with interest accrued thereon to July 1, 1938, shall be dealt with as follows: The Reconstruction Finance Corporation shall receive for the principal amount of its note and accrued unpaid interest approximately 90,255 1/2 shares of new no-par-value common stock and the right to subscribe for new first-mortgage bonds to be issued to provide new money; the Railroad Credit Corporation shall receive for the principal amount of its note and accrued unpaid interest, approximately 33,646 1/2 shares of new no-par-value common stock and the right to subscribe for new first-mortgage bonds to be issued to provide new money; and The A. C. James Company shall receive for the principal amount of its note and accrued unpaid interest approximately 35,560 shares of new no-par-value common stock and the right to subscribe for new first-mortgage bonds to be issued to provide new money.

(4) The unsecured claims of the Western Pacific Railroad Corporation and the Western Realty Company are found to be without value, and no securities or cash shall be distributed under the plan in respect to these claims.

(5) The capital stock of the debtor is found to be without equity or value, and the stockholders shall not be entitled to participate in the plan. [300]

(6) Current liabilities of the debtor incurred in the ordinary conduct of its business prior to the institution of this proceeding; current liabilities and

obligations of the debtor and its trustees incurred during this proceeding; and all other claims, liabilities, or obligations which have not hereinbefore been dealt with, are not to be affected by the plan, but to the extent that such claims, liabilities, or obligations are not paid by the debtor or its trustees pursuant to the order of the court, they shall be paid in cash or assumed by the reorganized company.

K. There will be issued to or on the orders of the Reconstruction Finance Corporation, Railroad Credit Corporation, and A. C. James Company, subscription warrants, in proportion to the general-mortgage bonds held by them, entitling the holders thereof to purchase at par, plus accrued interest, the \$10,000,000, principal amount, of new first-mortgage bonds to provide the new money in the reorganization. The warrants shall provide that they must be exercised within, but not later than, 45 days after the confirmation of the plan by the court. If any of these parties shall fail to subscribe for its full proportion, the other or others of such parties shall be entitled to subscribe for the unsubscribed balance in the proportion which the general-mortgage bonds held by them respectively bear to the total amount of general-mortgage bonds held by the parties so electing to subscribe for their full proportion. Should these parties fail to provide the new money in accordance with the above terms, holders of the debtor's first-mortgage bonds shall be entitled within 60 days of confirmation of the plan to provide the same upon the same terms and conditions as those provided for the aforesaid parties,

and appropriate subscription warrants will be issued to them. The holders of the warrants will be required to elect prior to the expiration of the warrants, in each case, the extent to which they will exercise their subscription rights.

In the event that none of the aforesaid creditors or the Reconstruction Finance Corporation subscribes for the bonds, a loan of \$10,000,000 shall be obtained from the Reconstruction Finance Corporation, secured by the pledge of such new first-mortgage bonds as division 4 of this Commission and the Reconstruction Finance Corporation may require in proceedings under section 5 [301] of the Reconstruction Finance Corporation Act. The purchase of any of the bonds by the Reconstruction Finance Corporation, or any loan by that Corporation upon such bonds as collateral will be subject to our approval under the provisions of the Reconstruction Finance Corporation Act.

L. A committee will be formed, after approval of the plan by this Commission and the court, with such power as may be necessary to carry out the plan, and to determine, subject to the approval of the court, the form and provisions of the indentures; bonds, stock certificates, and other instruments in connection with the carrying out of the plan. The committee shall consist of three members, one to be named by the first-mortgage bondholders, one by the Reconstruction Finance Corporation, Railroad Credit Corporation, and A. C. James Company, as a group, and the remaining member by the purchasers of the new first-mortgage bonds to be issued

to provide the new money in the reorganization, or if no commitment be received for the purchase of such bonds, by the party or parties advancing the new money necessary to retire the trustees' certificates.

M. The authority of the reorganization committee shall be auxiliary to, and supplementary of, the authority, powers, and duties of the debtor and any other corporation organized for the purpose of carrying out the plan to "put into effect and carry out the plan and the orders of the judge relative thereto, under and subject to the supervision and the control of the judge", as provided in section 77(f) of the Bankruptcy Act.

N. Existing mortgages on the debtor's properties shall be released and canceled, and all funds on deposit with the debtor's mortgage trustees representing sums paid from time to time to the trustees for the release of properties, sale of scrap, and otherwise, and all collateral pledged under the mortgage, shall be surrendered to the reorganized company free from existing mortgage liens, after deductions therefrom of any amounts which the court may find should be deducted under the provisions of the mortgages and consistent with the plan of reorganization herein approved. All collateral pledged by the debtor as security for its notes to the Reconstruction Finance Corporation, Railroad Credit Corporation, [302] and A. C. James Company, shall be surrendered to the reorganized company and canceled. The Railroad Credit Corporation also shall release and surrender the reorganized



company all its right and interest in the debtor's distributive shares under the marshaling and distributing plan, 1931, from and after the effective date of the plan, and any proceeds from such shares applied by the Railroad Credit Corporation to the payment of principal and/or interest of and upon the obligations of the debtor after the effective date of the plan, unless such application shall have been made by authority of the court of competent jurisdiction, shall be turned over to the reorganized company.

O. The approval and confirmation of the plan shall in no wise disturb or alter the right and interest of the Reconstruction Finance Corporation and the Railroad Credit Corporation in collateral pledged with them by parties other than the debtor.

P. Acceptance of the plan shall include acceptance of the new bonds, mortgages, stock certificates, and all instruments necessary and appropriate to the carrying out of the plan, other than the orders of the court and this Commission, to the same effect as though the terms of such instruments were set forth in full herein.

Q. The acceptance and confirmation of the plan, or the confirmation of the plan without acceptance, and the carrying of the plan, shall be provided in the Bankruptcy Act.

It is further ordered, That submission of the plan to the creditors for acceptance or rejection will be contingent upon the deposit with us in not more than 60 days after its approval by the court, of tentative commitments for the purchase of all of the

\$10,000,000 of new first-mortgage bonds to be issued under the plan, or within 75 days after such approval, a tentative commitment on the part of the Reconstruction Finance Corporation to make the required loan of \$10,000,000.

It is further ordered, That the authorization and approval herein granted by this Commission are upon the condition that the journal entries covering the necessary accounting adjustment under this order will be submitted to this Commission for approval before they are recorded on the books of the debtor or the reorganized company. [303].

It is further ordered, That nothing herein contained shall be, or be construed, as a grant of authority for the issue of any securities, assumption of obligations, transfer of any property, sale, consolidation, or merger of the debtor's property, or pooling of traffic, pursuant to either the Bankruptcy Act or the Interstate Commerce Act until further appropriate action by this Commission upon confirmation of the plan by the court.

By the Commission.

[Seal]

W. P. BARTEL,

Secretary.

A true copy.

W. P. BARTEL,

Secretary of the Interstate  
Commerce Commission.

[Endorsed]: Filed Oct. 21, 1938. [304]

300

*A. C. James Co. et al. vs.*

Interstate Commerce Commission

Finance Docket No. 10913

**WESTERN PACIFIC RAILROAD COMPANY  
REORGANIZATION**

**REPORT AND ORDER OF INTERSTATE  
COMMERCE COMMISSION IN PROCEED-  
ING UNDER SECTION 77 OF THE BANK-  
RUPTCY ACT.**

Submitted, January 20, 1939.

Decided, June 21, 1939. [307]

## TABLE OF CONTENTS

	Page of I. C. C. Report and Order	Page of This Printed Record
Report of the Commission.....	1	302
Opinion of Chairman Eastman, Concur- ing in Part.....	35	355
Opinion of Commissioner Miller, Con- curring in Part.....	36	357
Order of the Commission.....	40	362
		[308]

Upon further consideration, pursuant to appropriate petitions, plan for the reorganization of the Western Pacific Railroad Company modified and approved.\*

Appearances as in prior reports.

### REPORT OF THE COMMISSION ON FURTHER CONSIDERATION

By the Commission:

By our report and order issued October 10, 1938, in this proceeding, we approved a plan of reorganization of the Western Pacific Railroad Company, hereinafter called the debtor, pursuant to the provisions of section 77 of the Bankruptcy Act, as amended. 230 I.C.C. 61. On December 9, 1938, petitions for modification of our report and order of October 10, 1938, *supra*, were filed by the debtor, and the following interveners: Institutional Bondholders Committee, hereinafter called the bondholders committee; A. C. James Company, hereinafter called the James Company; Reconstruction Finance Corporation, hereinafter called the Finance Corporation; Railroad Credit Corporation, hereinafter called the Credit Corporation; and the Irving Trust Company, trustee under the debtor's general and refunding mortgage, hereinafter called the general-mortgage trustee. Under the provisions of section 77(d) of the Bankruptcy Act, as

---

\*Previous reports 207 I.C.C. 793, and 230 I.C.C. 61.



amended, we may, upon petition for good cause [309] shown filed within 60 days of the date of our order approving a plan, in a supplemental report and order modify any plan which we have approved. By our order of December 30, 1938, we reopened the proceeding for consideration of the modifications requested by the petitioners, and since additional evidence was not required for a consideration of the modification sought, we did not deem a further hearing necessary. The petitions for modification have been the subject of oral argument before us.

#### Requested Modifications

Under the modifications requested by the Credit Corporation, the effective date of the plan would be January 1, 1939, and the capitalization of the reorganized company would be comprised of \$2,750,050 of undisturbed equipment obligations, \$10,000,000 of first-mortgage 4-percent bonds, due 1989, \$20,901,240 of income-mortgage 4-percent bonds, due 2014, \$33,797,670, par value, of participating 5-percent preferred stock, \$14,190,318, par value, of participating 4-percent preferred stock, and 343,730 shares of common stock without par value.

Present holders of the debtor's first-mortgage bonds and the Finance Corporation would receive for the principal of their claims 40 percent thereof in new 4-percent income-mortgage bonds and 60 percent thereof in new 5-percent preferred stock,

and for the interest accrued and unpaid thereon 1 share of new 4-percent preferred stock for each \$100 thereof. The Credit Corporation would receive for the principal of its claim 100 percent thereof in new 5-percent preferred stock, and for the interest accrued and unpaid thereon 1 share of new 4-percent preferred stock for each \$100 thereof. The James Company would receive for the principal of its claim and for interest accrued and unpaid thereon new common stock at the rate of approximately 3 shares for each \$100 thereof. The Western Pacific Railroad Corporation and the Western Realty Company would receive for the principal of their claims and for interest accrued and unpaid thereon new common stock at the rate of approximately 2 shares for each \$100 thereof. The capital fund provided for in the approved plan would be decreased to \$300,000.

Counsel for the debtor concurred in the Credit Corporation's proposed modification on oral argument. [310]

The James Company requests that the capitalization provided for in the approved plan be substantially increased so that participation may be allowed to the debtor's unsecured creditors and stockholders in the reorganization but proposes no specific amount in its modifications. It further requests that the approved plan be modified to provide for the allocation to it, the Finance Corporation, and the Credit Corporation of new securities

on the basis of their respective claims rather than on the basis of the collateral pledged to secure the claims.

The bondholders committee incorporated its proposed modifications in a modified plan of reorganization and requests that such modified plan be approved by us in its entirety. The Finance Corporation concurs in the bondholders committee's modified plan.

Under the modified plan of the bondholders committee, the effective date of the plan would be January 1, 1939, and the capitalization of the reorganized company would be comprised of \$2,750,050 of undisturbed equipment obligations, \$10,000,000 of first-mortgage 4-percent bonds, series A, due 1964; \$20,901,240 of income-mortgage 4½-percent bonds, series A, due 2014, \$31,351,900 of participating 5-percent preferred stock, and 287,025 shares of common stock without par value.

Existing first-mortgage bondholders and the Finance Corporation would receive for the principal of their claims 40 percent thereof in new income mortgage bonds and 60 percent thereof in new preferred stock, and for interest accumulated and unpaid thereon new common stock equal to the amount of such interest, at the rate of \$66⅔ a share. The Credit Corporation would receive new common stock equal to the principal of its claim and interest accrued and unpaid thereon, taking the stock at a price of \$70 a share. The James Company would receive for the principal of its claim and interest

accrued and unpaid thereon an amount of new common stock which bears to the amount of common stock allotted to the claim of the Credit Corporation the same proportion that the principal amount of general and refunding bonds of the debtor held by the James Company as collateral for its claim bears to the principal amount of such bonds held by the Credit Corporation as collateral for its claim. Neither unsecured creditors nor stockholders would be entitled to participate in the reorganization.

The \$10,000,000 of new first-mortgage bonds would be sold at par and accrued interest to the Finance Corporation and the proceeds [311] thereof used to retire the \$10,000,000 of the debtor's trustees' certificates now held by the Finance Corporation. The purchase of these bonds at par is relied on as the consideration for the allocation to the Finance Corporation for the debtor's secured notes held by it of new securities of the same kind and amount as allotted to the holders of the debtor's existing first-mortgage bonds.

The modified plan of the bondholders committee also would modify and supplement the provisions in the plan approved in our prior report and order with respect to (1) the payment of interest and the date of maturity of the first-mortgage bonds, the issue of additional such bonds, and the lien of the first mortgage; (2) the rate of interest on the income-mortgage bonds, the issue of additional such bonds, and the lien of the income mortgage; (3) the

determination and application of available net income; (4) the issue of additional preferred stock, and the rights and interests of the holders of such stock; (5) the issue of additional common stock, and the rights and interests of the holders of such stock; (6) the claims not affected by the plan; (7) sale of the properties of the debtor at a fair upset price in the discretion of the court; (8) the capital fund; (9) the number, right of appointment, and functions of the reorganization managers; and (10) miscellaneous matters. These proposals will be more fully stated hereinafter.

The trustee under the debtor's general and refunding mortgage urges that there is such substantial value in certain assets pledged under the general and refunding mortgage as to which that mortgage admittedly constitutes a first lien as to require the allocation to the holders of the debtor's notes secured by general and refunding mortgage bonds a fair proportion of their claims in new securities of the same character as those allocated to the holders of the debtor's first-mortgage bonds.

#### Effective Date of the Plan

Under the plan approved in our prior report and order, the effective date of the plan would be July 1, 1938.

Conclusion.—Upon further consideration we approve January 1, 1939, as the effective date of the plan, and as the date from which interest shall run on the new securities provided in the plan. In view



of this modification, the modified plan will provide for the treatment of claims as of the effective date of the plan. [312]

### Capitalization and Charges

The outstanding capitalization of the reorganized company under the plan approved in our prior report and order would be comprised of \$3,066,117 of undisturbed equipment obligations, \$10,000,000 of first-mortgage 4-percent bonds, or a note for a like amount, \$19,716,040 of income-mortgage 4-percent bonds, \$29,574,060 of 5-percent preferred stock of the par value of \$100 a share, and 313,703 shares of common stock without par value.

Under the Credit Corporation's proposed modifications, the total funded debt of the reorganized company would be \$33,651,290 and the total annual fixed and contingent interest charges thereon, plus requirements for the capital and sinking funds proposed therein, would be \$1,734,758. Under the modified plan of the bondholders committee the total funded debt would be the same as under the Credit Corporation's plan but the total annual fixed and contingent interest charges, plus requirements for the capital and sinking funds, would be \$2,039,264. Under the Credit Corporation's modifications the new income bonds would bear interest at the rate of 4 percent per annum and the annual installment on the capital fund would be \$300,000 as compared to a rate of interest of 4½-percent on the income bonds and an annual installment of

\$500,000 on the capital fund proposed under the bondholders committee's modified plan.

In our prior report we stated that the total annual charges on the funded debt of the reorganized company, plus requirements of capital and sinking funds, should not exceed \$2,000,000, although the total of such amounts resulting under the provisions of the approved plan was only \$1,898,223. The income bonds provided for in the approved plan would bear interest at the rate of 4 percent per annum and the annual installment on the capital fund was fixed at \$500,000 with certain qualifications. We were influenced in fixing a rate of 4 percent on the income bonds in order to approve as large an amount of such bonds as we then considered practicable. The \$500,000 installment on the capital fund was based on the debtor's evidence that at least \$500,000 was needed for routine additions and betterments.

Conclusions.—We do not approve the decrease of capital fund installments from \$500,000 to \$300,000. Since the total funded [313] debt, including interest at  $4\frac{1}{2}$  percent on the income bonds, plus requirements of the capital and sinking funds, proposed under the bondholders committee's modified plan, plus the securities hereinafter provided for recognition of the first-lien position of the general and refunding bonds, would not result in charges materially exceeding \$2,000,000, we find that the reorganized company would be justified in issuing in consummation of the plan \$21,219,075 of income

mortgage 4½-percent bonds, and we will modify our previous report and order accordingly.

In our prior report we stated that the entire capital structure of the reorganized company must be realistically related to its actual earning power, and in determining such capital structure consideration should be given to the investment in the property only to the extent that such investment is justified by the probable earnings reasonably foreseeable for the future if the reorganization was to be successful. With these considerations in mind, and for the reasons there set forth, and upon consideration of the investment of the debtor in its property, the probable rate-making value thereof, and its traffic and earnings, we conclude that we cannot approve the total capital structure under the Credit Corporation's proposed modification. Upon further consideration of the above factors, however, we find that the issue by the reorganized company in the reorganization of 318,502 97/100 shares of 5-percent preferred stock of the par value of \$100 a share, and 319,441 shares of common stock without par value would be justified, and we will modify our prior report and order accordingly.

Under the above modifications the capitalization of the reorganized company upon reorganization will be comprised of \$2,750,050 of undisturbed equipment obligations, \$10,000,000 of first-mortgage 4-percent bonds, \$21,219,075 of income-mortgage 4½-percent bonds, \$31,850,297 of 5-percent pre-

ferred stock, and 319,441 shares of common stock without par value.

### ~~Provisions~~ for New Money

The plan approved in our prior report and order provides that the \$10,000,000 of first-mortgage bonds be sold at par, or, as an alternative, the borrowing of \$10,000,000 from the Finance Corporation, in order to secure funds to retire trustees' certificates out- [314] standing in the total amount of \$10,000,000. These certificates are now held by the Finance Corporation as collateral security for a loan of \$10,000,000. They rank equally and ratably with other expenses of administration and constitute a charge upon the estate prior to the claims of the first-mortgage bondholders and the secured noteholders. From representations of the intended purchasers and the possible lender, it appears that the most feasible method for obtaining the necessary \$10,000,000 is to provide for the purchase of the new first-mortgage bonds by the Finance Corporation. But the Finance Corporation is unwilling to purchase the bonds at par unless the payment of interest on them is made an immediate fixed charge instead of a contingent charge for the first five years as now provided in the approved plan. Our conclusion that the payment of interest on the bonds should be contingent for the first five years was based on the then current earnings of the debtor, and the possibility that the depressed business conditions then being experienced might continue.

Conclusions.—The present earnings justify the conclusion that the reorganized company should be able to meet the charges on the first-mortgage bonds. Under these circumstances, and in order to insure the raising of the new money which is absolutely necessary to effect a reorganization, we conclude and find that the interest on the first-mortgage bonds should be a fixed charge from the date of issue. We will modify our prior report and order accordingly, and will also provide that the Finance Corporation purchase the bonds at par and accrued interest and that in consideration of such purchase and the value of the collateral securing its claim, the Finance Corporation receive for the secured notes of the debtor held by it, treatment equal to that accorded the holders of the debtor's existing first-mortgage bonds. However, the proposed purchase of the new first-mortgage bonds or any part thereof by the Finance Corporation from the reorganized company is subject to and dependent upon our approval thereof in a separate proceeding.

#### Assets Pledged under the General and Refunding Mortgage

Upon further consideration, we also are of the opinion that *that the* value of the assets pledged under the general and refund- [315] ing mortgage upon which that mortgage admittedly constitutes a first lien requires a reexamination of the allocation of new securities to the holders of the debtor's notes



secured by the general and refunding mortgage bonds. These assets consist of cash in the hands of the mortgage trustee amounting to \$223,732, note of the Tidewater Southern Railway Company for \$508,278 representing that company's total funded debt, \$1,147,955, par value, of the capital stock of the Tidewater Southern, being about 97.5 percent of the total amount outstanding, \$270,000, principal amount, of bonds and \$360,834, par value, of stock of the Central California Traction Company, and \$465,300, par value, of the capital stock of the Alameda Belt Line.

Under section 19a of the Interstate Commerce Act, this Commission, by division 1, in Tidewater S. Ry. Co. 46 Val. Rep. 540, reported the value for rate-making purposes of the Tidewater Southern's property owned and used for common carrier purposes to be \$1,440,000 as of December 31, 1927. From December 31, 1927, to December 31, 1935, the carrier reported the net for additions and betterments, less retirements, to be \$168,882, and claims for items which were in existence, but omitted from the basic inventory to be \$1,910. Deducting depreciation accrued on equipment from January 1, 1928, to December 31, 1935, of \$4,184, as reported by the carrier, gives a net property change of \$166,608, which, if added to the final value for rate-making purposes, makes a total of \$1,606,608. In addition to the property owned and used for carrier purposes, the carrier owned and held for purposes other than those of a common carrier property the present value of

which was stated in the report, supra, to be \$272,951. The net additions and retirements on this class of property between January 1, 1928, and December 31, 1935, is reported as \$35,691. If these amounts be added to the total for common-carrier property, the total for property owned would be \$1,915,250. On the basis of the depreciation ratio of the property in 1927 the rate-making value as of December 31, 1935, plus the value of noncarrier property, would approximate \$1,850,000.

During the 6-year period 1930-35 the Tidewater Southern's earnings available for payment of interest averaged \$72,991 a year. In 1934 and 1935 such earnings were \$113,967 and \$114,512, respectively. During the same two years the debtor derived [316] revenues of \$549,069 and \$544,748, respectively, from traffic interchanged with the Tidewater Southern. For the 6-year period 1930-35 such revenues averaged \$532,820 a year.

The holdings of the debtor in the securities of the Central California Traction Company and the Alameda-Belt Line, which are pledged under the general and refunding mortgage, do not appear to be of much value, except as the debtor through such holdings may be able to secure traffic for its lines which it might not otherwise be able to secure. The Central California Traction Company's stock is owned equally by the debtor, the Atchison, Topeka & Santa Fe Railway Company, and the Southern Pacific Company. The parent companies have agreed to share equally any operating deficits or profits as

well as advances for bond interest, sinking fund, or additions and betterments. In 1934 and 1935, for example, the company reported net income of \$48,690 and \$6,314, but the parent companies contributed \$91,638 to the company in 1934 and \$61,373 in 1935. The stock of the Alameda Belt Line is owned in equal shares by the Atchison, Topeka & Santa Fe and the debtor. The parent companies have agreed to share equally any operating deficits or profits as well as advances for additions and betterments or other requirements. The parent companies contributed \$18,305 to the company in 1934 and \$27,727 in 1935. The company reported no net income in 1934 and \$480 in 1935. Thus the lien on the securities of these two companies has no material value.

**Conclusions.**—It is apparent that the Tidewater Southern is a paying railroad and also a valuable feeder for the debtor. But its earnings are, to a large extent, dependent upon the divisions of joint rates accorded it by the debtor. From the foregoing, it appears that the creditors secured by the general and refunding mortgage bonds should be awarded new income mortgage bonds in the amount of \$732,010, and new participating preferred stock of a par value of \$1,147,955. Applying to these amounts the proportionate amounts of general and refunding mortgage bonds securing the notes of the Finance Corporation, The Credit Corporation, and the James Company, the Finance Corporation would receive \$414,175 of income mortgage bonds and \$649,518

of new preferred stock, the Credit Corporation \$154,111 of income-mort- [317] gage bonds and \$241,681 of new preferred stock, and the James Company \$163,724 of income bonds and \$256,756 of new preferred stock for part of their claims. However, this allocation will apply only to the Credit Corporation and the James Company, for, as appears herein, we approve the allocation of new securities to the Finance Corporation on a different basis, i.e. on the basis upon which securities are allotted to the holders of existing first-mortgage bonds. In this connection we also find that such allocation of reorganization securities to the Finance Corporation exhausts the value of the collateral pledged by the debtor under the notes held by the Finance Corporation, and that the equity of the Credit Corporation in such collateral has no value.

The above modifications require further modification of our prior report and order with respect to the allocation of the reorganization securities. Under the modified capitalization there will be available for distribution among the creditors of the debtor, other than the holders of equipment obligations and trustees' certificates, \$21,219,075 of income mortgage bonds, \$31,850,297 of preferred stock, and 319,441 shares of no-par-value common stock. These securities represent the equitable equivalent of the debtor's assets available for the satisfaction of claims. The total of the claims of secured creditors other than the holders of equipment obligations and trustees' certificates, including interest accrued and

unpaid to January 1, 1939, amounts to \$75,138,610, and is comprised of the following: First-mortgage bondholders \$49,290,100 principal and \$13,143,777 interest; Finance Corporation \$2,963,000 principal and \$899,870 interest; Credit Corporation, \$2,445,610 principal and \$146,503 interest; and James Company \$4,999,800 principal and \$1,249,950 interest.

#### Conclusions in General as to Allotment of Securities

Based upon our conclusion as to the relative priority, value, and equity of the various claims and the value of the new securities available in exchange therefor, we find that the new securities should be allotted as follows: (1) First-mortgage bondholders, \$19,716,040 of income-mortgage bonds, \$29,574,060 of preferred stock, and 230,593 shares of common stock (the common stock to be taken at the price of \$57 a share); (2) Finance Corporation [318] \$1,185,200 of income-mortgage bonds, \$1,777,800 preferred stock, and 15,788 shares of common stock (the common stock to be taken at a price of \$57 a share); (3) Credit Corporation, \$154,111 of income mortgage bonds, \$241,681 preferred stock, and 35,425 shares of common stock, (the common stock to be taken at a price of \$62 a share); and (4) James Company, \$163,724 of income mortgage bonds, \$256,756 preferred stock, and 37,635 shares of common stock (being the amount of common stock which bears to the amount of common stock allotted to the claim of the Credit Corporation the same proportion that the principal amount of gen-



eral and refunding bonds of the debtor held by the James Company as collateral for its claim bears to the principal amount of such bonds held by the Credit Corporation for its claim). We will modify our prior report and order accordingly.

#### New First Mortgage and Bonds

Under the modified plan of the bondholders' committee the first mortgage would be a lien, subject only to liens upon equipment, on all properties and assets owned by the reorganized company on consummation of the plan, and all property acquired after reorganization, except that (a) if the reorganized company should acquire properties of any other company (except a company which is a wholly owned railway subsidiary on January 1, 1939) constituting a class 1 carrier, such properties would not be subject to the lien of the first mortgage unless acquired in whole or in part by the use of first-mortgage or income-mortgage bonds, or moneys deposited under those mortgages, and (b) if the reorganized company should be consolidated with, or merged into, or should sell its assets substantially as an entirety to any other class 1 carrier, no properties theretofore owned or thereafter acquired by such other company would be subject to the lien of the first mortgage except properties thereafter acquired which would be appurtenant or incident to properties subject to the lien of the first mortgage, or which would be within the maintenance or replacement covenants of the first mortgage, or which would be acquired by the use of first-mortgage or

income-bonds or moneys deposited under those mortgages. [319]

The amount of bonds issuable under the first mortgage would be limited to \$50,000,000. The mortgage would provide (1) that on each May 1 when the aggregate principal amount of first-mortgage bonds outstanding should equal or exceed \$20,000,000 the reorganized company would pay to the trustee under the mortgage as a sinking fund a sum equal to one-half of 1 percent of the maximum principal amount of such bonds theretofore at any one time authenticated and uncanceled; and (2) that on each May 1 when the aggregate principal amount of first-mortgage bonds outstanding plus all other funded debt bearing fixed interest should exceed either (a) 33 percent of the total capitalization of the reorganized company or (b) 50 percent of such total capitalization, less the principal amount of funded debt bearing contingent interest at the time outstanding, the reorganized company, in addition to the above-stated sums provided for the sinking fund for first-mortgage bonds, would pay into the sinking fund a sum equal to 50 per cent of the available net income of the next preceding calendar year that remains after providing for all income-mortgage sinking funds and charges prior thereto. Such sinking fund would be applied to the retirement of first-mortgage bonds, by purchase in the open market or by call for tenders at not exceeding the redemption price (or in case of bonds not redeemable; the principal amount and accrued inter-

est) and whenever the amount in the sinking fund exceeds \$50,000 and first-mortgage bonds are not tendered or cannot otherwise be purchased at less than their redemption price, the funds then in the sinking fund would be applied to the redemption of new first-mortgage bonds on the next succeeding interest payment date. All bonds so acquired would be canceled and no bonds would be issued to refund any such bonds. First-mortgage bonds and income-mortgage bonds outstanding would be deemed to include all bonds authenticated and delivered to the reorganized company which would not have been canceled or assured of retirement through the deposit of cash. Funded debt would include an amount equal to the capitalized value, at 5 percent per annum, of fixed rents payable for leased roads, other than terminal or bridge properties, but would not include (a) obligations (other than mortgage bonds or equipment-trust obligations) maturing not more than two years after their date, or (b) obligations of longer maturity secured by pledge [320] of bonds having a lien on property of the reorganized company except to the extent, if any, by which the principal amount of such obligations exceeds the principal amount of such bonds so pledged. Bonds guaranteed by the reorganized company as to interest or principal or both (other than bonds of a terminal or bridge company) would be included in funded debt, but, in case of a joint and several guaranty with other corporations, only to the extent of the reorganized company's basic obligation of the principal

liability. There would be included in determining total capitalization only (a) obligations constituting funded debt, (b) stock having par value, at such par value, and (c) stock without par value, at \$100 a share in case of the stock issuable under the plan, and, in case of other stock, at the capital value at which such stock is carried on the books of the company, not exceeding, however, (except to the extent that earned surplus would have been duly capitalized), the net amount received by the reorganized company on the issue thereof.

The first-mortgage bonds would be issuable in series, subject to such limitations and restrictions as may be specified in the first mortgage, payable on such date or dates, in such denominations, bearing interest at such rates and containing such provisions in regard to redemption, conversion, taxes, place or places and money or moneys of payment, registration, and sinking funds, and having such other characteristics as may be prescribed by the board of directors of the new company at the time of issue, but with respect to the lien of the first mortgage all equally secured, and \$10,000,000, series A, would be issued in the reorganization to provide the \$10,000,000 of new money required in the reorganization. So long as any of the series A bonds are outstanding no additional first-mortgage bonds would be issued having a maturity earlier than January 1, 1964. The series A bonds would be dated January 1, 1939, would mature January 1, 1964, would bear interest at 4 percent per annum, payable

semiannually, and would be redeemable, in whole or in part, at any time on 30 days' notice, at their principal amount and accrued interest, plus a premium of 3 per cent of their principal amount if redeemed on or before December 31, 1941,  $2\frac{1}{2}$  percent if redeemed thereafter and on or before December 31, 1945, 2 percent if redeemed thereafter and on or before December 31, 1949,  $1\frac{1}{2}$  percent if redeemed [321] thereafter and on or before December 31, 1953, 1 percent if redeemed thereafter and on or before December 31, 1957, and one-half of 1 percent if redeemed thereafter and on or before December 31, 1960, and without any premium if redeemed on or after January 1, 1961.

First-mortgage bonds, in addition to those authenticated in the reorganization, could be authenticated from time to time: (a) to refund first-mortgage bonds (excluding bonds issued solely by way of pledge, except as hereinafter stated) or outstanding obligations secured by first-mortgage bonds to the extent so secured or obligations secured by prior lien on after acquired property; or (b) upon the deposit of new cash equal to the principal amount to be issued; or (c) to provide for, or to reimburse the reorganized company for, not exceeding 75 percent of expenditures made after December 31, 1938, but not more than three years prior to the date of authentication (including expenditures ~~for the ac-~~quisition or construction of new railroad equipment, free from other lien, but not including expenditures for the making of additions and betterments to



equipment) which are properly chargeable to capital account under our accounting rules; provided, that (a) except when bonds are authenticated in respect of new mileage or in respect of new equipment, the 75 per cent would be applied to the net amount of such capital expenditures after deducting therefrom credits to capital account after December 31, 1938; (b) if any first-mortgage bonds are authenticated or cash deposited under the first mortgage is withdrawn to acquire railroad equipment, a sinking fund would be established, payable in equal annual installments sufficient to retire within the expected efficient service life of such equipment a principal amount of first-mortgage bonds equal to (1) the principal amount of bonds so authenticated or (2) the amount of deposited cash so paid; (c) if any property is acquired subject to existing liens the amount of additional first-mortgage bonds issuable therefor or issued to refund prior-lien obligations thereon, together with the aggregate amount of existing liens to which such property is subject, would not exceed 75 percent of the net cost thereof; and (d) no bonds would be issued on the basis of the acquisition of equipment under equipment-trust obligations or any obligations for the deferred payment of [322] the purchase price for equipment or on the basis of the retirement of any such obligations.

The first mortgage would contain a covenant to the effect that no first-mortgage bonds (other than those authenticated under the plan) would be sold

or pledged unless (1) the reorganized company should have contracted forthwith to sell or pledge such bonds and (2) two-thirds of the directors of the reorganized company should have determined that it was impracticable to provide the needed money (a) by the sale of income-mortgage bonds, or preferred stock, or common stock on specified terms and conditions. The first mortgage would also contain a covenant that the excess of the aggregate principal amount of all first-mortgage bonds under pledge at any one time over the principal amount of all indebtedness so secured would not exceed 10 per cent of the aggregate principal amount of all first-mortgage bonds then authenticated and uncanceled.

Conclusions:—Upon further consideration we find that the foregoing provisions with respect to the new first-mortgage bonds and the new first mortgage should be substituted for the corresponding provisions in our previous report and order, and we will modify our previous report and order accordingly, except that (1) the issue of all such bonds subsequent to the reorganization should be subject to our approval or to the approval of such regulatory body or tribunal as may have jurisdiction thereof; (2) the bonds of series A should be dated January 1, 1939, and should mature January 1, 1974; and (3) the premium payable in the event of their redemption should be at the following rates and on the following conditions: At the rate of 3 percent of **their principal amount if redeemed on or before De-**

cember 31, 1943, 2½ percent if redeemed thereafter and on or before December 31, 1948, 2 per cent if redeemed thereafter and on or before December 31, 1953, 1½ percent if redeemed thereafter and on or before December 31, 1958, 1 per cent if redeemed thereafter and on or before December 31, 1963, one-half of 1 per cent if redeemed thereafter and on or before December 31, 1968, and without any premium if redeemed on or after January 1, 1969. [323]

### Income Mortgage and Bonds

The income mortgage under the bondholders' committee's modified plan would constitute a lien, subject to the lien of the first mortgage, upon all property from time to time subject to the lien of the first mortgage. The income-mortgage bonds would be issuable, without limit as to aggregate amount or within such limit as might be specified in the income mortgage, from time to time in different series, subject to such limitations and restrictions as might be specified in the income mortgage, payable on such date or dates, in such denominations, bearing interest at such rates and containing such provisions in regard to accumulation of interest, redemption, conversion, taxes, place or places and money or moneys of payment, registration, and sinking funds, and having such other characteristics as may be prescribed by the board of directors of the new company at the time of issue, but with respect to the lien of the income mortgage all equally secured. No interest would be mandatorily payable on in-

come-mortgage bonds of any series (except at maturity or redemption) except out of available net income, as hereinafter provided. A total amount of \$20,901,240 of income-mortgage bonds would be authenticated and issued in the reorganization. The series A income bonds would be dated January 1, 1939, would mature January 1, 2014, would bear interest at the rate of  $4\frac{1}{2}$  percent per annum, due and payable as hereinafter stated and would be redeemable, in whole or in part, on May 1 in any year on 30 days' notice at their principal amount plus (a) full interest for the last preceding year and all unpaid accumulated interest for prior years and (b) interest at the rate of  $4\frac{1}{2}$  percent per annum from the last preceding December 31 to the redemption date. The series A bonds would be convertible into shares of common stock, as at the time constituted, at any time at the rate of 20 shares for each \$1,000, principal amount, of such bonds.

The interest on the series A income bonds, accruing for each calendar year would (up to the limits of accumulation hereinafter specified) become absolutely due as a debt on December 31 in such year, but would be payable on May 1 of the next succeeding year or thereafter as provided below. Such interest would be mandatorily payable (except as hereinafter stated) only out of [324] available net income remaining after providing for the capital fund hereinafter described and charges prior to the capital fund. All interest due and not paid on the next following May 1 would accumulate up to the

maximum amount of 13½ percent at any one time, but not beyond. Accumulated interest, within the limitations stated, would be mandatorily payable (a) whenever, and to the extent that, there is available net income for any subsequent year remaining after the deductions made pursuant to the provisions for the first-mortgage bond sinking fund, and the capital fund (in which case such amount would be paid on the next following May 1), or (b) in any event (whether earned or not) at the maturity or on redemption of the series A income bonds.

The income mortgage would provide for the payment on May 1 of each year while any series A income-mortgage bonds are outstanding of an installment of sinking fund, if earned, as, and in the amount hereinafter stated. Such installment would be payable only out of available net income for the last preceding calendar year that remains after meeting the requirements of the first mortgage bond sinking fund and the capital fund and payment of interest on outstanding income-mortgage bonds. The installment would equal (a) one-half of 1 percent of the principal amount of income-mortgage bonds, series A, theretofore at any one time authenticated and uncanceled, plus (b) an amount equal to interest on all income-mortgage bonds, series A, theretofore purchased or redeemed out of the sinking fund, calculated at the rate paid on such May 1 upon outstanding series A income-mortgage bonds. Accruals of such sinking fund installments would not be cumulative. The sinking



fund would be applied to the retirement of income-mortgage bonds, series A, by purchase in the open market or by call for tenders at not exceeding their redemption price, and whenever the amount in the sinking fund exceeds \$50,000 and income-mortgage bonds, series A, are not tendered or cannot otherwise be purchased at less than their redemption price, the funds then in the sinking fund shall be applied to the redemption of the income-mortgage bonds, series A, on the next succeeding interest payment date. All bonds so acquired shall be canceled and no bonds may be issued to refund any such bonds. Income-mortgage bonds in addition to those to [325] be issued at reorganization would be issuable from time to time to refund outstanding income-mortgage bonds or in lieu of first-mortgage bonds for the purposes and subject to the restrictions described as to the issue of additional first-mortgage bonds to the extent first-mortgage bonds are not issued for such purposes. No income-mortgage bonds, other than those to be issued in reorganization, could be issued, under the bondholders' committee's proposals, unless (1) the reorganized company shall have contracted forthwith to sell or pledge such bonds and (2) the board of directors of the reorganized company, by resolution adopted by two-thirds of the entire number of directors, shall have determined that, in the opinion of the board, taking into account market and all other relevant conditions at the time, it is impracticable to provide the amount of money needed (a) by the sale of pre-

ferred stock at a price which would give a current dividend return of 6 percent or less, or (b) by the sale of common stock at a price (not less than \$50 a share) which would give a dividend return (based on the regular dividend rate then in effect, or if no regular dividend rate is in effect, on the average rate at which dividends shall have been paid during the last 12 calendar months) of 6 percent or less. Provision would also be made in the mortgage substantially to the effect that the excess of the aggregate principal amount of all income-mortgage bonds under pledge at any one time over the principal amount of all indebtedness so secured should not exceed 10 percent of the aggregate principal amount of all income-mortgage bonds then authenticated and uncanceled. The mortgage would contain a further covenant for its modification and alteration and of the rights and obligations of the reorganized company and of the holders of the income-mortgage bonds, at any time by the concurrent action of the reorganized company and the holders of not less than  $66\frac{2}{3}$  percent in aggregate principal amount of the bonds then outstanding, but the covenant would contain a proviso that no such change or modification would alter or impair the obligation of the reorganized company to pay the principal of any bond without the consent of the holder of such bond.

° *Conclusions.*—Upon further consideration we approve the foregoing provisions relative to the income mortgage and bonds, except that (1) \$21,219,-

075 of such bonds should be issued in [326] the reorganization; and (2) the issue of income-mortgage bonds subsequent to the reorganization should be subject to our approval or to the approval of such regulatory body or tribunal as may have jurisdiction thereof. We find that the provisions so modified should be substituted for the corresponding provisions in our previous report and order.

#### Determination and Application of Available Net Income

Available net income under the bondholders' committee's modified plan would be determined for each calendar year beginning with the year 1939, and continuing thereafter so long as any income-mortgage bonds remain outstanding.

Available net income for each calendar year would be determined by deducting all fixed charges of the reorganized company and its wholly owned railway subsidiaries accrued during such calendar year from the consolidated income of the reorganized company and its wholly owned railway subsidiaries available for fixed charges for such calendar year (determined in accordance with our accounting rules). It would be provided, however, that if the reorganized company should not come into ownership and possession of the properties now operated by the debtor's trustees on or before January 1, 1939, available net income for any period after January 1, 1939, until the reorganized company comes into ownership and possession of such properties, would be computed

as if the reorganized company had come into such ownership and possession on January 1, 1939, and had issued as of that date, the new securities issuable under the plan, other than the \$10,000,000 of new first-mortgage bonds, series A, and in lieu of interest on such bonds there would be charged the amount of interest actually accruing during such period upon any then outstanding trustees' certificates or other obligations issued to provide funds for rehabilitation purposes.

Available net income would be ascertained for each such calendar year, as the accounts would be stated on the books of the reorganized company during such calendar year, without adjustments, except that (1) in determining available net income there would not be deducted any amounts from the proceeds of the trustees' certificates issued for rehabilitation purposes, notwithstanding [327] standing that under our accounting rules such expenditures may be chargeable as operating expenses; (2) if in respect of any calendar year the available net income is a deficit, the amount of the deficit may, in the discretion of the reorganized company, be carried forward and deducted in determining available net income for the succeeding calendar year or calendar years until such deficits (or accumulated deficits) be extinguished by earnings which in the absence of such deficits would be available net income; and (3) debits or credits to adjust income in prior years would be treated as income items for the year in which entered on the books, whether

cleared through income or profit and loss accounts, so far, but only insofar, as such debits and credits reflect cash receipts or disbursements in the year in which they are entered on the books.

Available net income for each calendar year would be applied to the following purposes and in the following order:

(1) To the creation, if and when the aggregate principal amount of first-mortgage bonds outstanding should equal or exceed \$20,000,000, of the sinking fund hereinbefore described in connection with the first-mortgage indenture, in an amount up to, but not exceeding, in any calendar year, one-half of 1 percent of the maximum principal amount of first-mortgage bonds theretofore at any one time authenticated and uncanceled.

(2) If the directors of the reorganized company in their discretion should so determine, available net income of each calendar year may be applied to the creation of a capital fund to be applied to, or to provide for, or to reimburse the treasury for, capital investments, as defined by our Classification of Income, Profit and Loss, and General Balance Sheet Accounts for Steam Railroads, Accounts Nos. 701, 702, and 705 (or advances to subsidiaries for expenditures, which, if made directly by the reorganized company in respect of its owned or leased properties, would be charged to such accounts), or such substituted accounts as may at the time be in effect, to the extent that such capital investments have been made or contracted for during such cal-



endar year or within three months thereafter, and including therein (but only to the extent that such payments during such calendar year shall exceed depreciation of equipment charged against income for such calendar [328] year) payments made for new equipment, or initial and principal payments upon equipment leased under equipment trusts or purchased under conditional-sale agreements and installments of sinking funds proposed in the event proceeds of additional first-mortgage bonds are issued in the purchase of equipment, provided, however, that

(a) The amount set aside in the capital fund should not exceed \$500,000 in respect of any calendar year, or such lesser sum as may be required, together with unappropriated accumulations in the fund as of the close of the calendar year prior to that for which the payment is to be computed, less charges for additions and betterments during such calendar year for which payment is to be computed, to bring the total in the fund to \$1,000,000; provided, however, that the capital fund should not exceed \$1,000,000 at any one time;

(b) The capital funds may be applied only to such part of the cost of the capital investments as hereinbefore defined as remains after deducting from such cost all retirements of roadway and structures charged against income in such calendar year; and

(c) To the extent that expenditures are so provided for or reimbursed out of the capital fund, the company would not thereafter have the right to issue any bonds or other evidence of indebtedness or any stock ranking, as to either assets or dividends, in priority to, or on a parity with, the preferred stock of series A to capitalize or reimburse such expenditures; provided, however, that such expenditures may, within such limits, if any, as may be specified in the first mortgage or the income mortgage, be used to supply the excess of capital expenditures required to be certified under either mortgage over the principal amount of the bonds that may be issued under the terms thereof; and

(3) Any then remaining available net income for any calendar year would be applied to the payment on the next succeeding May 1 of interest on the then outstanding income mortgage bonds (not including any thereof held in the sinking fund) accrued during the last preceding calendar year, and of any accumulated unpaid interest thereon.

(4) Any then remaining available net income for any calendar year would be applied to the payment of the sinking fund installment provided for the income bonds, series A. [329]

(5) Any then remaining net income for any calendar year might be applied to the creation of a sinking fund for income-mortgage bonds of series

other than A, if any such sinking fund should have been provided for at the time of the creation of any such series.

(6) Any then remaining available net income for any calendar year would be applied to the payment of the installment, if any, then due under the sinking fund provided in the event first-mortgage bonds are outstanding in excess of certain limits.

(7) Any then remaining available net income for any calendar year may be applied to any proper corporate purpose of the reorganized company (except dividends on the new common stock), including, if and to the extent that such dividends are declared by the directors, the payment of dividends upon the preferred stock in respect of such year and of any accrued and unpaid cumulative dividends on the preferred stock.

(8) Any then remaining available net income for any calendar year may be applied to any proper corporate purpose of the reorganized company, including dividends on common stock (but only after all accrued and unpaid cumulative dividends on the preferred stock have been paid).

No interest would need to be paid on income-mortgage bonds if the amount to be paid is less than one-fourth of 1 percent. Any excess available for interest but not paid because of the foregoing provision would be reserved and added to income available for interest on the income-mortgage bonds for the next succeeding calendar year.

If there are outstanding income-mortgage bonds of different series, the amount applicable to interest

on such bonds would be distributed among the respective series in proportion to the unpaid interest at the time accumulated on the bonds of such series, respectively.

Dividends could be paid on stock of any class (subject to the relative rights of the several classes of stock) out of the income of any calendar year prior to the close of such calendar year if, but only if, prior to the declaration of such dividends, the directors should have determined that the available net income [330] for such year applicable for the purposes specified in the foregoing paragraphs (1), (3), (4), (5), and (6) would be more than sufficient to pay the amounts payable out of such available net income pursuant to such paragraphs and such amounts should have been deposited in trust for the purposes specified in such paragraphs. Dividends on common stock would be so declared only if, prior to such declaration, the directors should have determined that the applicable part of available net income for such year would be more than sufficient to pay the amount hereinabove specified for dividends (including accumulations) on the preferred stock and such amount should have been deposited in trust for the purpose of paying such dividends.

Conclusions.—In our opinion payments into the capital fund should be mandatory upon the board of directors and the plan should so provide. It should also provide that the amount required to be set aside for the capital fund each calendar year be \$500,000

less amounts charged during the calendar year to operating expenses in respect of retirements of road property, and in respect of depreciation of road property if reserves for depreciation of road property be established, provided that the amount in the capital fund at the end of the calendar year, including the amount set aside for the fund in respect of that calendar year, should not exceed \$1,000,000. The plan should further provide that the capital fund may be applied only to such part of the cost of capital investments defined in the foregoing proposals as remains after deducting from such cost the amounts charged to operating expenses for retirement of road property and all amounts charged to operating expenses for any reserves for depreciation of road property that may be established. In all other respects we find that the foregoing provisions for the determination and application of available net income should be substituted for the corresponding provision in our previous report and order.

### Preferred Stock

Under the modified plan of the bondholders committee, preferred stock would be authorized in the total amount of 750,000 shares each of the par value of \$100, of which 313,519 shares of series A would be issued in the reorganization. The additional [331] authorized preferred stock not issued in the reorganization would be issuable from time to time in the discretion of the board of directors of the reorganized company, but (unless for the purposes



for which first-mortgage bonds might otherwise have been issued) only after the concurring vote or consent of the holders of a majority of the outstanding preferred stock. So far as permitted by law, such additional preferred stock would be of series A, or of any other series, one or more, and preferred stock of any such other series might bear dividends at such rate, cumulative or noncumulative, might be redeemable or nonredeemable, convertible or nonconvertible, and might have such other rights and privileges and be subject to such limitations and restrictions, as should be from time to time determined by the board of directors prior to the issue of preferred stock of any such other series. If there should be outstanding shares of preferred stock of different series, the earnings applicable to dividends thereon would be apportioned among the respective series in proportion to the dividends accumulated on the shares of such series respectively. In any liquidation or winding up of the reorganized company, whether voluntary or involuntary, the preferred stock would be entitled to receive, out of the assets of the reorganized company, its par value, plus any accrued and unpaid cumulative dividends thereon, plus such premium, if any, as may be specified for any series, before any distribution would be made on the common stock, but would not be entitled to any further participation in such assets. Holders of preferred stock would be entitled to one vote per share on all matters, except that in the elections of directors, which would be by cumu-

lative voting, each holder of stock of either class would be entitled to as many votes per share as the number of directors to be elected. The reorganized company could not, without the vote or consent of the holders of at least two-thirds in par value of the outstanding new preferred stock,

(1) Create or permit to be created any mortgage or other lien upon any of the properties, excepting the new first mortgage, the new income mortgage, or purchase-money liens (including equipment obligations) upon property hereafter acquired, given for not more than 75 percent of the purchase price of such property; [332]

(2) Create or issue any bonds, notes, or other evidence of indebtedness maturing more than two years from their date, except new first-mortgage bonds and new income-mortgage bonds and except purchase-money obligations given for not more than 75 percent of the purchase price of the property hereafter acquired;

(3) Create any stock ranking either as to assets or dividends, in priority to, or on a parity with, the new preferred stock, or

(4) Permit any subsidiary, all of the stock of which except directors' shares, shall be owned by the reorganized company, to create any mortgage or lien upon any of its properties or issue any bonds, notes, or other evidences of indebtedness or any additional stock, unless the obligations secured by such mortgage or other lien or such other obligation or such stock would be acquired by the reorganized company.

The preferred stock, series A, would be entitled to receive all accumulated unpaid dividends and current dividends at the rate of 5 percent per annum in respect of any calendar year before any dividends could be paid or declared or set apart for payment on the common stock in respect of such year. Such dividends would be cumulative to the extent earned in any calendar year but not paid; but such dividends would otherwise be noncumulative. For the purposes of the next preceding sentence herein above, preferred stock dividends would be considered to be earned in any calendar year to the extent covered by available net income for such year that remains after providing for prior charges. After dividends shall have been paid or declared on the new common stock at the rate of \$3 a share in respect of any calendar year, each share of preferred stock, series A, would be entitled to share equally with each share of new common stock in any dividends paid or declared in respect of such year. The preferred stock, series A, would be redeemable, in whole or in part, at any time at its par value plus accrued and unpaid cumulative dividends, and proportionate dividend for the current year. The holders of preferred stock, series A, would not have any preemptive right to subscribe to any additional issues of stock of any class or of securities convertible into stock of any class.

Conclusion.—We find that the foregoing provisions should be substituted for corresponding provisions of our previous report [333] and order, ex-

cept that (1) 318,502 97/100 shares of preferred stock, series A, should be issued in the reorganization; and (2) no preferred stock, after reorganization, should be issued without our approval or the approval of such regulatory body or tribunal as may have jurisdiction thereof.

### Common Stock

Under the modified plan of the bondholders committee, common stock would be authorized in the total amount of 1,000,000 shares, without par value, of which 287,025 shares would be issued in the reorganization and 418,026 shares would be reserved for the conversion of income-mortgage bonds, series A. Holders of common stock would be entitled to one vote on all matters except that directors would be elected by cumulative voting.

Conclusion.—We find that the foregoing provisions should be substituted for the corresponding provisions of our prior report and order, except that (1) 319,441 shares of common stock should be issued in the reorganization and 424,382 shares should be reserved for the conversion of income-mortgage bonds, series A; and (2) no new common stock additional to that actually issued in connection with the reorganization shall be issued without our approval or the approval of such regulatory body or tribunal as may have jurisdiction thereof.

### Claims Not Affected by the Plan

The modified plan of the bondholders committee would provide that the following claims would not

be affected by the plan: (a) Current liabilities of the debtor incurred in the ordinary conduct of its business prior to the institution of the reorganization proceeding, which are entitled to priority over one or more of the mortgages of the debtor, and (b) current liabilities and obligations of the debtor's trustees incurred during the reorganization proceeding. It would further provide that to the extent that such claims, liabilities, or obligations are not paid by the debtor or its trustees pursuant to order of the court, they would be paid in cash or assumed by the reorganized company. All such claims, liabilities, and obligations may be adjusted or compromised [234] and dealt with or paid or discharged by the reorganized company, all as may be determined by the directors of the reorganized company subject to approval by the court. The reorganized company would be deemed to have assumed such of the contracts of the debtor which are executory in whole or in part, including any executory leases and liabilities under guaranties, as shall have been affirmed by the debtor's trustees with the approval of the court prior to the date of confirmation of the plan, and also any executory contracts made by the debtor's trustees with the approval of the court which, by their terms, do not terminate at the conclusion of the reorganization proceeding.

Conclusions.—We are unable to approve all of the foregoing provisions. The plan should provide that claims *against* the debtor entitled to priority over any mortgage of the debtor, current liabilities,



and obligations incurred by the trustees of the properties of the debtor during the reorganization proceeding, and expenses of reorganization allowed by the court within the maximum fixed by us should be paid in cash or assumed by the reorganized company, provided that any amounts so assumed by the reorganized company shall constitute a charge upon the properties of the reorganized company prior in lien to all new securities issued under the plan. When so treated, we find that claims against the debtor entitled to priority over any mortgage of the debtor are not affected by the plan. We further find that the claims of the holders of the debtor's equipment-trust certificates, and obligations under the Baldwin lease and Pullman contract are not materially and adversely affected by the plan. The plan should further provide that the reorganized company should be deemed to have assumed the executory contracts of the debtor which by their terms do not terminate at or prior to the conclusion of the reorganization proceeding and which shall have been affirmed or shall not have been disaffirmed by the trustees; with the approval of the court, prior to the confirmation of the plan and also any executory contracts made by the trustees with the approval of the court which by their terms do not terminate at or prior to the conclusion of the reorganization proceeding. The plan also should provide that the reorganized company will assume the liability for, and will pay in full in due course, any and all taxes due to the United States from the debtor or the

debtor's trustees [335] for any taxable period prior to the date of the confirmation of the plan, whether or not proof thereof has been made in this proceeding and without prejudice by reason of not having made proof thereof. We will modify our previous report and order accordingly.

### Method of Executing the Plan

Under the bondholders' committee's modified plan, existing mortgages on the debtor's properties would be released and canceled, and all funds on deposit with the trustees under the debtor's mortgages representing sums paid from time to time for the release of properties, sale of scrap, and otherwise, and all collateral pledged under the mortgages, would be surrendered to the reorganized company free from liens of the debtor's mortgages, after deductions therefrom of any amounts which the court may find should be deducted under the provisions of such mortgages and consistent with the plan. All collateral pledged by others than the debtor as security for the debtor's notes to the Finance Corporation, Credit Corporation, and James Company, would be surrendered to the pledgors thereof, and all collateral pledged by the debtor as security for such notes would be reduced to possession by the respective pledgees thereof, and would then be by them surrendered to the reorganized company and canceled, except that the Credit Corporation would not release or surrender any right or interest in the distributive shares of the debtor or its subsidiaries

under the marshaling and distributing plan, 1931, but any proceeds from such distributive shares after the effective date of the plan, would become the property of and be retained by the Credit Corporation, but to the extent to which received prior to the issue of the new securities under the plan would be applied in reduction of the claim of the Credit Corporation.

Conclusion.—We do not approve that part of the foregoing provisions which states that all collateral pledged by others than the debtor as security for the debtor's notes to the Finance Corporation, Credit Corporation, and James Company would be surrendered to the pledgors thereof. With this provision eliminated we approve the foregoing provisions. The court by orders of March 11, 1936, and March 20, 1936, authorized the Chase Na- [336] tional Bank of the City of New York to pay from funds which had been deposited with it by the debtor all outstanding first-mortgage bond coupons which matured on or prior to September 1, 1933, and had not theretofore been presented for payment. In the absence of later information it is assumed that not all of these coupons will have been presented at the consummation of the reorganization and that the plan should make provision for them. Our order of approval of a plan will provide that such coupons shall be paid in cash by the new company if and when presented by the holders thereof.

Under the bondholders' committee's modified plan, the plan would be carried out under the supervision of a reorganization committee consisting of five persons, three of whom would be designated by holders of existing first-mortgage bonds in such manner as we may prescribe, one by the Finance Corporation, and one by the Credit Corporation and the James Company jointly. The plan would be carried out either by revesting the properties formerly of the debtor in the debtor or by transferring such properties to a new corporation organized for the purpose, and the execution by the corporation in which such properties are vested of the new mortgages and the issue by it of the new securities contemplated by the plan. The method of carrying out the plan would be determined by the reorganization committee in its discretion, and the reorganization committee would also determine, subject to the approval of the court, the form and, except as otherwise expressly provided in the modified plan, the provisions of all mortgages, bonds, coupons, charters, by-laws, stock certificates, voting trust certificates, acceptances, assents, and all other instruments in the judgment of the reorganization committee necessary or desirable in connection with carrying out the plan. The reorganization committee would act by a majority of its members as from time to time constituted, at a meeting or in writing without a meeting. The reorganization committee could from time to time delegate to others any power or discretion conferred upon it by the plan; and the

members of the committee would not be liable for any action taken by them in good faith or by any person employed by the committee in good faith, except for their respective individual malfeasance or wilful neglect. [337]

**Conclusions.**—Upon further consideration, we find that the foregoing provisions respecting the appointment and functions of the reorganization committee and the carrying out of the plan should be substituted for the corresponding provisions in our prior report and we will modify our previous report and order accordingly except that

(1) The reorganization committee should consist of three persons, all to be approved by the court, one of whom should be designated by the bondholders committee, one by the Finance Corporation, and one by the Credit Corporation and the James Company jointly. Should the bondholders committee, or the Finance Corporation, or the Credit Corporation and the James Company jointly, fail to designate a representative for membership on the committee within such time as the court considers reasonable, the court should appoint such a representative.

(2) Should the reorganization committee solicit deposits of securities, or authorization to represent holders of the debtor's existing securities in the reorganization, the terms and conditions upon which such solicitation and representation would be made should be subject to our prior approval.



The modified plan of the bondholders committee would provide that in case any class of creditors or stockholders does not accept the plan, any party in interest would have the right to move the court to confirm the plan on the ground that the interests of such class of creditors have no value, or that the equity of such class of stockholders has no value, or on the ground that the plan provides for the payment in cash to such class of an amount not less than the value of their interests or equity, if any, in accordance with subsection (e) of section 77, through the sales described in the following paragraph in accordance with clause (5) of subdivision (b) of section 77:

If so ordered by the court the plan would be executed by a sale at public auction, at not less than a fair upset price as determined by the court, of all, or any part of the properties and assets of the debtor, free from all liens or claims, other than those expressly stated in the plan not to be affected by the plan. Upon any such sale the properties and assets offered for sale may be purchased for the benefit of the reorganized company by the reor-  
[338] ganization committee, or by a purchaser nominated by the reorganization committee, and in that event there would be applied on account of the purchase price the distributive share, if any, of the proceeds of such sale of all securities the holders of which should have accepted the plan, and the securities, though not accepting the plan, of all classes which, as a class, have accepted the plan in accord-

ance with section 77. All properties and assets so sold which are purchased by the reorganization committee would be transferred to the reorganized company. In the event of any such sale, the reorganization committee might in its discretion sell all or any portion of the new securities distributable under the plan in respect of the securities of any creditor, if neither such creditor nor the class to which such creditor belongs should have accepted the plan in accordance with section 77. The proceeds of any such sale, together with any other funds, which in the judgment of the reorganization committee are available among the assets of the debtor estate or of the reorganized company, might be used to pay the portion of the purchase price payable in cash on any such sale. Upon any such sale, nonassenting secured creditors of any class, which, as a class, should not have accepted the plan in accordance with section 77 and the unsecured creditors and the stockholders of either class, would be entitled to receive, in lieu of the securities, if any, otherwise issuable under the plan, their aliquot proportion of the proceeds of such sale, after deducting therefrom all expenses of such sale and the amount which would be required to pay in full, or principal and unpaid interest accrued to the date of such sale, all creditors whose claims are prior in lien or superior in equity to the claims of such nonassenting secured creditors or the rights of such unsecured creditors or stockholders. If any properties and assets are purchased at any such sale by others than

the reorganization committee, security holders having an interest in such properties and assets would be entitled, in accordance with the priorities of their respective interests, to receive, in lieu of such securities, if any, issuable to them, their aliquot portion of the proceeds of the sale of such property and assets, after deducting therefrom all expenses of such sale. In such event the reorganization committee would, with the approval of this Commission and the court, make such modification in the plan as may be appropriate under the circumstances.

[339]

In our prior report we declined, for reasons stated therein, to approve a provision in the plan for the public sale of the property at a fair upset price. The foregoing terms and conditions for such a sale, however, are materially different from those proposed originally. Under the foregoing provision, the determination as to whether a sale should be had would be in the discretion of the court.

**Conclusions.**—Since, in our opinion, the plan of reorganization approved herein conforms to the requirements of section 77, and believing that the public interest would be promoted by an early consummation of this proceeding, we approve the substance of the foregoing provisions respecting the sale of the debtors' properties, but not all of the detailed provisions proposed in connection therewith. We approve the following in lieu of the foregoing provisions:

If deemed desirable and so ordered by the court, the plan, after it has been found fair and equitable

and confirmed by the court, may be executed by a sale at not less than a fair upset price to be fixed by the court, of all or any part of the property of the debtor, all on such conditions and in such manner as the court may direct. Upon any such sale the property and assets offered for sale may be purchased for the benefit of the reorganized company by the reorganization committee, and in that event there shall be applied on account of the purchase price the distributive share of the proceeds of such sale of all securities the holders of which shall have assented to the plan, and of the securities, though not assenting to the plan, of all classes which shall have accepted the plan.

In the event of a sale of the properties of the debtor to the reorganization committee, the committee may in its discretion sell all or any portion of the new securities, if any, distributable under the plan to holders of existing securities, if neither such security holder nor the class to which such security holder belongs shall have accepted the plan, provided that security holders in a class which shall not have accepted the plan, and who themselves shall not have accepted the plan shall have the right, if they shall so notify the committee within a period of 30 days after the confirmation of such sale, to assent to the plan and receive the securities allocated to them under the plan in lieu of their aliquot share of [340] the proceeds of such sale of the properties. The proceeds of any such sale of securities may be used to pay the portion of the purchase

price payable in cash on any such sale of the properties.

#### Method of Giving Notice

The modified plan of the bondholders committee provides that unless otherwise provided in section 77 or any order or orders of the court or of this Commission, whenever notice would be required or permitted to be given under or pursuant to the plan, such notice should be given by publishing a copy of such notice once in each week on any secular day in each such week for two successive weeks in one newspaper published and of general circulation in the Borough of Manhattan, City and State of New York, and in one newspaper published and of general circulation in the City of San Francisco, State of California, and also (1) in case of notices to security holders who have accepted the plan, by mailing such notice to such security holders at the addresses set forth in the acceptances signed by them; and (2) in case of notices to security holders who shall not have accepted the plan, by mailing such notice to such security holders whose names and addresses appear on the books of the debtor or of the reorganized company, as the case may be, but failure to mail any such notices, would not invalidate the notice by publication above provided for, which alone would be sufficient.

Conclusion.—We approve the foregoing provisions and will incorporate them in the modified plan.



### Expenses of the Reorganization

The bondholders' committee's modified plan provides that all expenses in connection with the plan and its consummation, and all costs of administration and other allowances made by the court would be paid by the reorganized company, subject to the provisions of section 77, and would constitute a charge upon the properties of the reorganized company as a cost of administration prior in lien to all new securities issued under the plan. There would be included in such expenses such reasonable compensation for necessary services rendered and reimbursement for actual expenses incurred in connection with the reorganization [341], proceeding and the plan by the trustees under the mortgages, the reorganization committee, the bondholders committee, and other parties in interest and the attorneys or agents of any thereof, as may be approved by this Commission and the court pursuant to section 77, but no compensation would be paid to members of the bondholders committee for their services as such members.

Conclusion.—In view of the definite provisions of section 77 relative to allowances for compensation and expenses of a reorganization, and in view of the other provisions of the plan, we see no necessity for including the foregoing provisions in the plan and, therefore, do not approve them.

### Management

Under the modified plan of the bondholders' committee the board of directors of the reorganized company would consist of not less than 7 nor more than 11 members, who would be elected by the stockholders of the reorganized company at an election to be held not later than 90 days after the consummation of the plan. Pending such election the board of directors would consist of such persons as may be designated by the reorganization committee with the approval of the court.

Conclusion.—We find that the foregoing provisions should be incorporated in the modified plan.

### General Conclusions

We find that the plan of reorganization approved in our report and order of October 10, 1938, *supra*, modified as herein indicated, will meet with the requirements of section 77 (b) and (e) of the Bankruptcy Act, as amended, and will be compatible with the public interest.

In view of the provisions of section 77(f), we will give consideration, when a plan is finally adopted, to the granting of such authorizations as may be requisite and appropriate for the execution of the plan, including the issue of securities.

The authorization and approval herein granted by us should be upon the condition that the journal entries covering the necessary accounting adjustments under such authorization and approval

should be submitted to us for approval before they are recorded [342] on the books of the reorganized company under the plan of reorganization herein approved.

An appropriate order, superseding our order of October 10, 1938, in this proceeding, will be entered.

---

Eastman, Commissioner, concurring in part:

For the reasons indicated in my expression of partial concurrence in connection with the prior report in this proceeding, 230 I.C.C. 81, 107, I do not favor the provision for a mandatory capital fund.

Nor am I satisfied with the following provision of the report:

(2) if in respect of any calendar year the available net income is a deficit, the amount of the deficit may, in the discretion of the reorganized company, be carried forward and deducted in determining available net income for the succeeding calendar year or calendar years until such deficits (or accumulated deficits) be extinguished by earnings which in the absence of such deficits would be available net income;

It seems to me that this provision should be mandatory and should not be left to the discretion of the railroad management.

While I do not dissent from other provisions of the plan, I venture to add a word of comment in

regard to one problem which has engaged much attention in the consideration of this and other reorganization plans. It is recognized that it is one thing to bring a railroad out of bankruptcy with a sound financial structure and quite another thing to keep the structure sound for the future. There are, broadly speaking, two ways to promote the latter result. One way is to incorporate more or less automatic safeguards in the plan, in the way of mortgage limitations upon the issue of bonds, capital funds, sinking funds, and the like. The other way is to rely upon a sound and intelligent management of the company as a first line of defense, and upon sound and intelligent regulation by this Commission as a second line of defense.

The difficulty with the first way is that it is impossible to foresee all contingencies of the future, and rigid provisions of the automatic type may, on this account, prove of dubious benefit under some conditions, if not of actual harm. While I by no [343] means oppose all such provisions, they do not impress me as being entirely satisfactory.

The second way ought to be the better way. Its weakness lies in the frailties of human beings. In one respect neither the Commission nor the managements made a very distinguished record for soundness and intelligence in connection with the issue of railroad securities in the decade which preceded the depression. The record was not so bad as some think, for there were notable issues of stock, and the ratio of indebtedness to total in-

vestment for the railroads in the aggregate decreased materially, but I think it cannot be denied that insufficient advantage was taken of opportunities to issue stock in preference to bonds, and that too little foresight was exhibited in this respect. I am hopeful, however, that experience has taught its lesson and that the managements may be counted upon as a more effective safeguard for the future against the development of unsound financial structures than they have proved to be in the past, and I am confident that this will be true of the Commission.

---

Miller, Commissioner, concurring in part:

As stated in my dissent to our previous decision in this case (Western Pacific Reorganization, 230 I.C.C. 61), I do not agree with the provision for a mandatory capital fund. I am also unable to agree that the stockholders of the old company are not entitled to participate in the reorganization. If capitalization were based on the original cost of the property less depreciation, as I also suggested in the decision referred to above, the stockholders could be given an opportunity to participate to some extent in the future profits, if any, either with or without a cash contribution as might be appropriate.

While I do not feel warranted at this time nor at this stage of the proceedings in connection with the reorganization of this road, in dissenting upon



any other points, I do wish to draw attention to certain questions which this plan raises in my mind. All these questions are closely related to the possibility that under this plan the future financing of the Western Pacific will be done primarily by expanding fixed interest debt. Although the junior income indenture under the present plan has quite properly been opened up for future financing, we still permit the increase of fixed interest [344] first mortgage bonds up to a total of 50 million dollars. This permission, when considered in connection with the par value of the preferred stock, the cumulation of income bond interest and the covenants relating to the issuance of the first mortgage bonds, strengthens an impression that this plan may facilitate the creation of first mortgage fixed interest debt and militate against financing by junior incomes and capital stock.

The par value provision naturally tends to prevent the preferred stock from being sold at less than par, while the provision for the accumulation of interest charges on the income bonds, even though only a partial one, will tend to prevent the preferred stock price from reaching a par level.

The new plan attempts to guard against the over-issue of fixed interest bonds by requiring that whenever the fixed interest debt of the corporation exceeds 35 percent of the total capitalization of the reorganized company or 50 percent of such total capitalization less the principal amount of contin-

gent interest funded debt, the corporation shall pay into the sinking fund 50 percent of the available net income of the preceding calendar year after providing for all income mortgage sinking funds and charges prior thereto, such fund to be applied to the amortization of the first mortgage bonds.

The total capitalization of the company, taking the no par common stock at \$100 per share, has been fixed at \$97,763,522. The fixed interest debt is \$12,750,050. The total capitalization less the present fixed interest debt, therefore, is \$85,013,472. If neither the income bonds, other debt, nor the stock are increased, the first mortgage fixed interest debt may be expanded to a total of \$45,776,485, or 35 percent of a total capitalization of \$130,789,957 before the penalty sinking fund under the 35 percent of total capitalization covenant becomes effective. On similar assumptions the total fixed interest debt, including these bonds, may rise to a higher total before the penalty sinking fund under the 50 percent of total capitalization less the contingent interest debt becomes operative.

Although the amortization of the income bonds is to begin immediately under the plan, no sinking fund is provided for the first mortgage fixed interest debt until or unless the amount of such debt is double the 10 million dollars of first mortgage bonds presently to be issued. [345]

The lien and the earning capacity of the income bonds and consequently their availability for financing would no doubt be greatly improved (1) by

the limitation of the first mortgage issue to 10 million or perhaps a slightly larger amount to provide for emergencies, and (2) by the requirement of sinking fund payments on the first mortgage bonds at a rate sufficiently high to eliminate them from the capitalization at a comparatively early date. The sinking fund payments on the income bonds might be postponed for a time in order to increase those on the first mortgage debt, and the amounts to be paid to the capital fund could be diverted to the same purpose.

If the preferred stock were made a no par issue and the cumulative feature of the income bonds eliminated, the availability of the former for future financing would presumably be greatly enhanced. The loss of protection from the elimination of the cumulative feature might be compensated by giving the bondholders in its place a participation in the earnings after income bond interest, such participation to be applicable only in so far as the specified rate has not been paid on the incomes in any and all prior years.

The proposed restriction on the issuance of fixed interest first mortgage bonds would appear to imply that it is the amount of fixed interest debt in relation to the capitalization which determines the ability of the corporation to meet fixed interest payments. Is it not rather the amount of fixed interest in relation to the earnings which determines the ability of the corporation to meet its interest charges? Certainly the question may be raised as

to whether the sounder method of checking the undue expansion of fixed interest debt does not lie in covenants restricting the expansion of that debt in terms of demonstrated capacity to meet fixed interest charges during the immediately preceding years. Nor would it be necessary to make this earnings type of covenant less elastic than the one now proposed. Although we have jurisdiction over the future issuance of securities by this road, an indenture limitation on the issuance of bonds in terms of the relation of fixed interest obligations to total capitalization is no less a restriction of our jurisdiction than a similar limitation framed in terms of adequate coverage of interest charges by the earnings. [346]

The amortization of the first mortgage bonds could be begun immediately. If the bonds were limited, as indicated above, to the amount presently to be issued or slightly higher, the sinking fund payments should be fixed at whatever percentage of the earnings (estimated as nearly as possible) after fixed or contingent interest is calculated to redeem the entire debt in some limited period of years. If the mortgage were left open up to 50 million dollars, the percentage of earnings after fixed or after contingent interest, as might be determined, should be so adjusted that the sinking fund payments would progressively increase with the expansion of borrowing to an extent sufficient to redeem all the first mortgage bonds by maturity regardless of the

extent or frequency of first mortgage borrowing in the meantime.

Aitchison, Commissioner, did not participate in the disposition of this case. [347]

---

### ORDER

At a General Session of the Interstate Commerce Commission, held at its office in Washington, D. C., on the 21st day of June A. D. 1939,

Finance Docket No. 10913

Western Pacific Railroad Company Reorganization

It appearing, That this Commission, by its report and order of October 10, 1938, approved a plan of reorganization for the debtor; and

It further appearing, That upon the filing of petitions by the debtor and five other interveners, requesting that certain modifications be made in the approved plan, the proceeding was reopened and oral argument was heard on the question of such proposed modifications; and

It further appearing, That the Commission upon reconsideration of the record herein in the light of the aforesaid argument, has, on the date hereof, made and filed its supplemental report containing its findings of fact and conclusions thereon with respect to the modifications of plan requested, and a full statement of the reasons therefor, which



report is hereby referred to and made a part hereof:

It is hereby ordered, That the following plan of reorganization of the aforesaid debtor be, and it is hereby, approved:

Terms used herein shall have the following meanings, respectively:

The debtor.—The Western Pacific Railroad Company;

Consummation of the plan.—The transfer to the reorganized company, to the extent contemplated by the plan, of the properties and assets of the debtor.

Court.—The District Court of the United States for the Northern District of California, Southern Division. [348]

Effective date of the plan.—The date from which interest shall run on the new securities provided in the plan, namely, January 1, 1939.

First-mortgage bonds.—Bonds issued under the first mortgage dated June 26, 1916, from the company to the First Federal Trust Company and Henry E. Cooper, as trustees (Crocker First National Bank and Samuel Armstrong successor trustees), designated as the first mortgage.

General and refunding bonds.—Bonds issued under the mortgage dated January 1, 1932, from the company to the Chase National Bank of the City of New York as trustee (Irving Trust Company now successor trustee), designated as the general and refunding mortgage.

Reorganized company.—The corporation, whether the debtor or a new corporation, which shall acquire substantially all of the properties now held by the bankruptcy trustees and issue the new securities provided for by the plan.

A. The effective date of said plan shall be January 1, 1939.

B. The capitalization of the reorganized company, upon consummation of the plan, shall consist substantially of undisturbed equipment trusts, Baldwin lease, and Pullman contract, \$2,750,050; new first-mortgage 4-percent bonds \$10,000,000; new income-mortgage 4½-percent bonds \$21,219,075; new 5-percent preferred stock \$31,850,297; new common stock without par value 319,441 shares.

C. The first-mortgage bonds shall be secured by a first mortgage, which will be a lien, directly or through pledge of securities, subject only to liens upon equipment, on all the properties and assets owned by the reorganized company on the consummation of the plan, including securities, equipment, and the equity in such equipment as is subject to equipment obligations. The first mortgage will also be a lien on all similar property acquired by the reorganized company after the reorganization, except that (a) if the reorganized company shall acquire the properties of any other company (except a company which is a wholly owned railway subsidiary on January 1, 1939) constituting a class I carrier as defined by the rules of this Commission or other public regula- [349] tory bodies having

jurisdiction at the time, such properties shall not be subject to the lien of the first mortgage unless acquired in whole or in part by the use of first-mortgage bonds or income-mortgage bonds, or moneys deposited under the first mortgage or the income mortgage, and (b) if the reorganized company shall be consolidated with, or shall be merged into, or shall sell its assets substantially as an entirety to, any other company which at the time is a class I carrier defined as aforesaid, no properties theretofore owned or thereafter acquired by such other company shall be subject to the lien of the first mortgage except properties thereafter acquired which shall be appurtenant or incident to properties subject to the lien of the first mortgage, or which shall be within the maintenance or replacement covenants of the first mortgage, or which shall be acquired in whole or in part by the use of first-mortgage bonds or income-mortgage bonds or moneys deposited under the first mortgage or the income mortgage.

D. The amount of bonds issuable under the first mortgage will be limited to \$50,000,000.

The first mortgage will provide (1) that on each May 1 when the aggregate principal amount of first-mortgage bonds outstanding shall equal or exceed \$20,000,000, the reorganized company will pay to the trustee under the first mortgage as a sinking fund a sum equal to one-half of 1 percent of the maximum principal amount of first-mortgage bonds theretofore at any one time authenticated and

uncanceled; and (2) that on each May 1 when the aggregate principal amount of first-mortgage bonds outstanding plus all other funded debt bearing fixed interest shall exceed either (a) 35 percent of the total capitalization of the reorganized company, determined as hereinafter provided, or (b) 50 percent of such total capitalization, less the principal amount of funded debt bearing contingent interest at the time outstanding, the reorganized company, in addition to the sums provided in this subdivision D to be paid, will pay into said sinking fund a sum equal to 50 percent of the available net income of the next preceding calendar year that remains after providing for all income mortgage sinking funds and charges prior thereto (i. e., that remains after the deductions made pursuant to subparagraphs (1), (2), (3), (4), and (5) of of the fourth paragraph of subdivision L hereof; or after the [350] provisions of said subdivision L shall have ceased to be operative, 50 percent of net income as defined by the accounting rules or practice referred to in said subdivision L). Such sinking fund shall be applied to the retirement of first-mortgage bonds, by purchase in the open market or by call for tenders at not exceeding the redemption price (or in the case of bonds not redeemable, the principal amount and accrued interest); and whenever the amount in the sinking fund exceeds \$50,000 and first-mortgage bonds are not tendered or cannot otherwise be purchased at less than their redemption price, the funds then in

the sinking fund shall be applied to the redemption of new first-mortgage bonds on the next succeeding interest payment date. All bonds so acquired shall be canceled, and no bonds may be issued to refund any such bonds. First-mortgage bonds and income-mortgage bonds outstanding shall be deemed to include all bonds authenticated and delivered to the reorganized company which shall not have been canceled or assured of retirement through the deposit of cash. Funded debt shall include an amount equal to the capitalized value, at 5 percent per annum, of fixed rents payable for leased roads, other than terminal or bridge properties, but shall not include (a) obligations, other than mortgage bonds or equipment-trust obligations, maturing not more than two years after their date, or (b) obligations of longer maturity secured by pledge of bonds having a lien on property of the reorganized company except to the extent, if any, by which the principal amount of such obligations exceeds the principal amount of such bonds so pledged. Bonds guaranteed by the reorganized company as to interest or principal or both, other than bonds of a terminal or bridge company, shall be included in funded debt, but, in case of a joint and several guaranty with other corporations, only to the extent of the reorganized company's basic proportion of the principal liability. There shall be included in determining total capitalization only (a) obligations constituting funded debt, (b) stock having par value, at such par value, and (c) stock without



par value, at \$100 a share in case of the stock issuable under the plan, and, in case of other stock, at the capital value at which such stock is carried on the books of the company, not exceeding, however (except to the extent that earned surplus shall have been duly capitalized), the net amount received by the reorganized company on the issue thereof. [351]

E. The first-mortgage bonds may be issued from time to time in different series, subject to the approval of this Commission or the approval of such regulatory body or tribunal as may have jurisdiction thereof, and to such limitations and restrictions as may be specified in the first mortgage, payable on such date or dates, in such denominations, bearing interest at such rates and containing such provisions in regard to redemption, conversion, taxes, place or places and money or moneys of payment, registration, and sinking funds and having such other characteristics as may be prescribed by the board of directors of the reorganized company at the time of issue, but with respect to the lien of the first mortgage all equally secured. So long as any first-mortgage bonds, Series A, shall be outstanding no additional first-mortgage bonds shall be issued having a maturity earlier than January 1, 1974.

F. Ten million dollars first-mortgage bonds, series A, are to be authenticated and issued in the reorganization for the purpose of providing the \$10,000,000 of new money required in the reorganization.

The bonds of series A shall be dated January 1, 1939, shall mature January 1, 1974, shall bear interest at the rate of 4 percent per annum, payable semiannually, and shall be redeemable, in whole or in part, at any time on 30 days' notice, at their principal amount and accrued interest, plus a premium of 3 percent of their principal amount if redeemed on or before December 31, 1943; 2½ percent if redeemed thereafter and on or before December 31, 1948, 2 percent if redeemed thereafter and on or before December 31, 1953, 1½ percent if redeemed thereafter and on or before December 31, 1958, 1 percent if redeemed thereafter and on or before December 31, 1963, one-half of 1 per cent if redeemed thereafter and on or before December 31, 1968, and without any premium if redeemed on or after January 1, 1969.

G. First-mortgage bonds, in addition to those to be authenticated in the reorganization, may be authenticated from time to time, subject to the approval of this Commission or such regulatory body or tribunal as may have jurisdiction thereof; (a) to refund first-mortgage bonds (excluding bonds issued solely by way of pledge, except as hereinafter provided) or outstanding obligations secured [352] by first-mortgage bonds to the extent so secured or obligations secured by prior lien on after acquired property; or (b) upon the deposit of new cash equal to the principal amount to be issued; or (c) to provide for, or to reimburse the reorganized company, for, not exceeding 75 percent of expenditures made after December 31, 1938, but not more than three

years prior to the date of such authentication (including expenditures for the acquisition or construction of new railroad equipment, free from other lien, but not including expenditures for the making of additions and betterments to equipment) which, under the accounting rules of this Commission or other Federal regulatory bodies having jurisdiction in the premises, at the time in force, are properly chargeable to capital account; provided, however, that

(a) Except when bonds are authenticated in respect of new mileage (or securities representative thereof) or in respect of new equipment, the said 75 percent shall be applied to the net amount of said capital expenditures after deducting therefrom, to such extent and on such basis as may be specified in the first mortgage, credits to capital account after December 31, 1938;

(b) If any first-mortgage bonds are authenticated or cash deposited under the first mortgage is withdrawn to provide or reimburse for the acquisition of railroad equipment, a sinking fund shall be established (in addition to any other sinking fund then in effect for any series of first-mortgage bonds) payable in equal annual installments in an amount sufficient to retire (at par) within the expected efficient service life of such equipment (in no case to exceed 15 years) a principal amount of first-mortgage bonds equal to (1) the principal

amount of bonds so authenticated or (2) the amount of deposited cash so paid;

(c) If any property is acquired subject to existing liens the amount of additional first-mortgage bonds issuable therefor or issued to refund prior-lien obligations thereon, together with the aggregate amount of existing liens to which such property is subject, shall not exceed 75 percent of the net cost thereof, including as part of such cost the amount of such existing liens whether or not the indebtedness secured thereby is assumed by the reorganized company; and

(d) No bonds shall be issued on the basis of the acquisition of equipment under equipment-trust obligations or any [353] obligations for the deferred or serial payment of the purchase price for equipment, or on the basis of the retirement of any such obligations.

H. The first mortgage will contain a covenant substantially to the effect that no first-mortgage bonds (other than those to be authenticated under the plan) will be sold or pledged unless (1) the reorganized company shall have contracted forthwith to sell or pledge such bonds and (2) the board of directors of the reorganized company, by resolution adopted by two-thirds of the entire number of directors, shall have determined that, in the opinion of the board, taking into account market and all other relevant conditions at the time, it is impracticable to provide the amount of money needed (a) by the

sale of income-mortgage bonds having a maturity of 20 years or more at a price which would give a yield to maturity of 5 percent or less, or (b) by the sale of preferred stock at a price which would give a current dividend return of 6 percent or less, or (c) by the sale of common stock at a price (not less than \$50 a share) which would give a current dividend return (based on the regular dividend rate then in effect, or, if no regular dividend rate is in effect, on the average rate at which dividends shall have been paid during the last twelve calendar months) of 6 per cent or less.

The first mortgage will also contain a covenant substantially to the effect that the excess of the aggregate principal amount of all first-mortgage bonds under pledge at any one time over the principal amount of all indebtedness so secured shall not exceed 10 percent of the aggregate principal amount of all first-mortgage bonds then authenticated and uncanceled.

I. The income mortgage shall constitute a lien, subject to the lien of the first mortgage, upon all property from time to time subject to the lien of the first mortgage.

The income-mortgage bonds may be issued, without limit as to aggregate amount or within such limit as may be specified in the income mortgage, from time to time in different series, subject to the approval of this Commission or such regulatory body or tribunal as may have jurisdiction thereof, and subject to such limitations and restrictions as



may be specified in the income mortgage, payable on such date or dates, in such denominations, bearing interest [354] at such rates and containing such provisions in regard to accumulation of interest, redemption, conversion, taxes, place or places and money or moneys of payment, registration, and sinking funds, and having such other characteristics as may be prescribed by the board of directors of the reorganized company at the time of issue, but with respect to the lien of the income mortgage all equally secured. No interest shall be mandatorily payable on income-mortgage bonds of any series (except at maturity or redemption) except out of available net income, as hereinafter provided.

J. Twenty-one million two hundred nineteen thousand seventy-five dollars of income-mortgage bonds, series A, are to be authenticated and issued in the reorganization, as set out in subdivision P below.

The income-mortgage bonds of series A shall be dated January 1, 1939, shall mature January 1, 2014, shall bear interest at the rate of  $4\frac{1}{2}$  percent per annum, due and payable as hereinafter provided, and shall be redeemable, in whole or in part, on May 1 in any year, on 30 days' notice, at their principal amount plus (a) full interest for the last preceding year and all unpaid accumulated interest for prior years and (b) interest at the rate of  $4\frac{1}{2}$  percent per annum from the last preceding December 31 to the redemption date.

The income-mortgage bonds of series A shall be convertible into shares of common stock, as at the time constituted, at any time at the rate of 20 shares per \$1,000, principal amount, of such bonds.

Interest on income-mortgage bonds, series A, accruing for each calendar year shall (up to the limits of accumulation hereinafter specified) become absolutely due as a debt on December 31 in such year, but shall be payable on May 1 of the next succeeding year or thereafter as provided below. Such interest shall be mandatorily payable (except as hereinafter provided) only out of available net income of the reorganized company that remains after providing for the capital fund and charges prior thereto (i.e., that remains after the deductions made pursuant to subparagraphs (1) and (2) of the fourth paragraph of subdivision L). All interest that comes due and is not paid on the next following May 1 shall accumulate up to the maximum amount of 13½ percent at any one time; but not beyond. Accumulated interest shall be mandatorily payable (a) whenever, and to the extent that, there is available net income [355] for any subsequent year remaining after the deductions made pursuant to said subparagraphs (1) and (2) of the fourth paragraph of subdivision L (in which case such amount shall be paid on the next following May 1), or (b) in any event (whether earned or not) at the maturity or on redemption of the income-mortgage bonds of series A. For the purposes of the two sentences next hereinabove, payments of

interest shall be considered as applied to interest accrued for the last preceding calendar year before being applied to accumulations. The board of directors of the reorganized company may at any time, in its discretion, pay any interest accrued on the income-mortgage bonds, series A, even if not earned, out of any funds lawfully available therefor.

The income-mortgage will provide for the payment on May 1 of each year while any income-mortgage bonds, series A, are outstanding, of an installment of the sinking fund, if earned, as, and in the amount, hereinafter specified. Such installment shall be payable only out of available net income for the last preceding calendar year that remains after paying interest on outstanding income-mortgage bonds (i.e., that remains after the deductions made pursuant to subparagraphs (1), (2) and (3) of the fourth paragraph of said subdivision L). The amount of such installment shall equal (a) one-half of 1 percent of the maximum principal amount of income-mortgage bonds, series A, theretofore at any one time authenticated and uncanceled, plus (b) an amount equal to interest on all income-mortgage bonds, series A, theretofore purchased or redeemed out of the sinking fund, calculated at the rate paid on said May 1 upon outstanding income-mortgage bonds of series A. Such accruals of the sinking-fund installments shall not be cumulative. The sinking fund shall be applied from time to time to the retirement of income-mortgage bonds, series A, by purchase in the open market or by call for tenders

at not exceeding their redemption price, and whenever the amount in the sinking fund exceeds \$50,000 and income-mortgage bonds, series A, are not tendered or cannot otherwise be purchased at less than their redemption price, the funds then in the sinking fund shall be applied to the redemption of the income-mortgage bonds, series A, on the next succeeding interest payment date. All bonds so acquired shall be canceled and no bonds may be issued to refund any such bonds. [356]

Income-mortgage bonds, in addition to those to be issued in the reorganization, may be issued from time to time, subject to the approval of this Commission or of such regulatory body or tribunal as may have jurisdiction thereof, to refund outstanding income-mortgage bonds or in lieu of first-mortgage bonds, for the purposes and subject to the restrictions stated in respect of the issue of additional first-mortgage bonds above, to the extent that first-mortgage bonds are not issued for such purposes.

K. No income-mortgage bonds (other than those to be issued under the plan) may be authenticated and delivered unless (1) the reorganized company shall have contracted forthwith to sell or pledge such bonds and (2) the board of directors of the reorganized company, by resolution adopted by two-thirds of the entire number of directors, shall have determined that, in the opinion of the board, taking into account market and all other relevant conditions at the time, it is impracticable to provide the amount

of money needed (a) by the sale of preferred stock at a price which would give a current dividend return of 6 percent or less, or (b) by the sale of common stock at a price (not less than \$50 a share) which would give a current dividend return (based on the regular dividend rate then in effect, or, if no regular dividend rate is in effect, on the average rate at which dividends shall have been paid during the last 12 calendar months) of 6 percent or less.

The income mortgage will also contain a covenant substantially to the effect that the excess of the aggregate principal amount of all income-mortgage bonds under pledge at any one time over the principal amount of all indebtedness so secured shall not exceed 10 percent of the aggregate principal amount of all income-mortgage bonds then authenticated and uncanceled.

The income mortgage will provide, within conditions and limits to be therein prescribed, for the modification and alteration thereof and of the rights and obligations of the reorganized company and of the holders of the income-mortgage bonds thereunder, at any time by the concurrent action of the reorganized company and of the holders of not less than  $66\frac{2}{3}$  percent in aggregate principal amount of the bonds then outstanding; provided, however, that no such change or modification shall alter or impair the obligation of the reorganized company to pay the principal of any bond without [357] the consent of the holder of such bond. In the event of any unification of the properties of the reorganized com-



pany with the properties of any other company, the modifications hereinabove authorized may include provisions excluding in whole or in part the earnings from such other properties in determining available net income and providing for the determination of such available net income without the maintenance of separate accounts.

L. Available net income shall be determined for each calendar year beginning with the year 1939, and continuing thereafter so long as any income-mortgage bonds remain outstanding. When no income-mortgage bonds remain outstanding, the provisions of this subdivision L shall cease to be operative.

Available net income for each such calendar year shall be determined by deducting all fixed charges of the reorganized company and its wholly owned railway subsidiaries accrued during such calendar year from the consolidated income of the reorganized company and its wholly owned railway subsidiaries available for fixed charges for such calendar year (determined in accordance with the accounting rules of this Commission or other analogous Federal authority having jurisdiction in the premises at the time in force, or, to the extent not governed by such accounting rules, in accordance with sound accounting practice); provided, however, that if the reorganized company shall not come into ownership and possession of the properties now operated by the bankruptcy trustees on or before January 1, 1939, available net income for any period after January 1, 1939, until the reorganized com-

pany comes into ownership and possession of such properties shall be computed as if the reorganized company had come into such ownership and possession on January 1, 1939, and had issued, as of that date, the new securities issuable under the plan, other than the \$10,000,000 of new first-mortgage bonds, series A, and in lieu of interest on such bonds there shall be charged the amount of interest actually accruing during such period upon any then outstanding trustees' certificates or other obligations issued to provide funds for rehabilitation purposes.

Available net income shall be ascertained for each such calendar year as the accounts shall be stated on the books of the reorganized company during such calendar year, without adjust- [358] ments, except that (1) in determining available net income there shall not be deducted any amounts from the proceeds of the trustees' certificates issued for rehabilitation purposes, notwithstanding that under the accounting rules hereinbefore mentioned such expenditures may be chargeable as operating expenses; (2) if in respect of any calendar year the available net income is a deficit, the amount of such deficit may, in the discretion of the board of directors of the reorganized company, be carried forward and be deducted in determining available net income for the succeeding calendar year or calendar years until such deficit (or accumulated or remaining deficits) be extinguished by earnings which in the absence of such deficit or deficits, would be available net income; and (3) debits or credits to

adjust income in prior years shall be treated as income items for the year in which entered on the books, whether cleared through income or profit and loss accounts, so far but only insofar, as such debits and credits reflect cash receipts or disbursements in the year in which they are entered on the books.

Available net income for each calendar year shall be applied to the following purposes and in the following order:

(1) To the creation, if and when the aggregate principal amount of first-mortgage bonds outstanding shall equal or exceed \$20,000,000, of the sinking fund provided for in subdivision D hereinabove, in an amount up to, but not exceeding, in respect of any calendar year, one-half of 1 percent of the maximum principal amount of first-mortgage bonds theretofore at any one time authenticated and uncanceled.

(2) To the creation of a capital fund to be applied to, or to provide for, or to reimburse the treasury of the reorganized company for, capital investments, as defined by this Commission's Classification of Income, Profit and Loss and General Balance Sheet Accounts for Steam Roads, Accounts Nos. 701, Investment in road and equipment, 702, Improvements on leased railway property, and 705, Miscellaneous physical property (or advances to subsidiaries for expenditures which, if made directly by the reorganized company in respect of its owned or

leased properties, would be charged to said accounts), or such substituted accounts as may at the time be in effect, to the extent that such capital investments have been made or contracted for during such calendar year or within three months thereafter, and including therein but only to [359] the extent that such payments during such calendar year shall exceed depreciation of equipment charged against income for such calendar year) payments made for new equipment, or initial and principal payments upon equipment leased under equipment trusts or purchased under conditional-sale agreements and installments of sinking fund provided for by subparagraph (b) of subdivision G (relating to first-mortgage bonds issued for equipment), provided, however, that

(a) The amount set aside in the capital fund each calendar year shall be \$500,000 less amounts charged during the calendar year to operating expenses in respect of retirements of road property, and in respect of depreciation of road property if reserves for depreciation of road property be established, provided that the amount in the capital fund at the end of the calendar year, including the amount set aside for the fund in respect of that calendar year, shall not exceed \$1,000,000.

(b) The capital fund may be applied only to such part of the cost of capital investments as hereinabove defined as remains after deducting from such cost the amounts charged

to operating expenses for retirement of road property and all amounts charged to operating expenses for any reserves for depreciation of road property that may be established.

(c) To the extent that expenditures are so provided for or reimbursed out of the capital fund, the company shall not thereafter have the right to issue any bonds or other evidences of indebtedness or any stock ranking, as to either assets or dividends, in priority to, or on a parity with, the preferred stock of series A to capitalize or reimburse such expenditures; provided, however, that such expenditures (if for purposes for which first-mortgage bonds or income-mortgage bonds may be issued) may, within such limits, if any, as may be specified in the first mortgage or the income mortgage, be used to supply, in whole or in part, the excess of capital expenditures required to be certified under either such mortgage over the principal amount of the bonds that may be issued under the terms thereof; and

(3) Any then remaining available net income for any calendar year shall be applied to the payment on the next succeeding May 1, of interest on the then outstanding income-mortgage bonds (not including any thereof then held in any sinking fund) accrued during the last preceding calendar year, and of any accumulated unpaid interest thereon. [360]



(4) Any then remaining available net income for any calendar year shall be applied, so long as any income mortgage bonds, series A, are outstanding, to the payment on the next succeeding May 1, of the sinking fund installment provided for in subdivision J (relating to income-mortgage bonds, series A).

(5) Any then remaining available net income for any calendar year may be applied to the creation of a sinking fund for income-mortgage bonds of series other than series A, if any such sinking fund shall have been provided for at the time of the creation of any such series.

(6) Any then remaining available net income for any calendar year shall be applied to the payment on the next succeeding May 1 of the installment, if any, then due under the sinking fund provisions of subdivision D hereinabove (relating to first-mortgage bonds when outstanding in excess of certain limits).

(7) Any then remaining available net income for any calendar year may be applied to any proper corporate purpose of the reorganized company (except dividends on the new common stock), including, if and to the extent that such dividends shall be declared by the board of directors of the reorganized company, the payment of dividends upon the preferred stock in respect of such year and of any accrued and unpaid cumulative dividends on the preferred stock; such dividends to be paid, except as here-

inafter provided, on such date or dates in the next succeeding year as may be specified in the certificate of incorporation or by-laws of the reorganized company, or in the certificates for the preferred stock.

(8) Any then remaining available net income for any calendar year may be applied to any proper corporate purpose of the reorganized company, including (but only after all accrued and unpaid cumulative dividends on the preferred stock to the end of such year shall have been paid, or declared and set apart for payment) dividends on the common stock.

No interest need be paid on income-mortgage bonds if the amount to be paid is less than one-fourth of 1 percent. Any excess available for interest but not paid because of the foregoing provision shall be reserved and added to the income available for interest on the income-mortgage bonds for the next succeeding calendar year. [361]

If there are outstanding income-mortgage bonds of different series, the amount applicable to interest on such bonds shall be distributed among the respective series in proportion to the unpaid interest at the time accumulated on the bonds of such series, respectively.

Dividends may be paid on stock of any class (subject to the relative rights of the several classes of stock) out of the income of any calendar year prior to the close of such calendar year if, but only if, prior to the declaration of such dividends, the board

of directors shall have determined that the available net income for such year applicable for the purposes specified in the foregoing paragraphs (1), (2), (3), (4), (5), and (6) will be more than sufficient to pay the amounts payable out of such available net income pursuant to said paragraphs and such amounts shall have been deposited in trust for the purposes specified in said paragraphs. Dividends on common stock may be so declared only if, prior to such declaration, the board of directors shall have determined that the applicable part of available net income for such year will be more than sufficient to pay the amount hereinabove specified for dividends (including accumulations) on the preferred stock and such amount shall have been deposited in trust for the purpose of paying such dividends.

M. There will be authorized 750,000 shares of preferred stock, each of the par value of \$100, of which 318,502 97/100 shares of series A are to be issued in the reorganization as set out in subdivision P below.

The additional authorized preferred stock not issued in the reorganization will be issuable from time to time, subject to the approval of this Commission, or of such regulatory body or tribunal as may have jurisdiction thereof, in the discretion of the board of directors of the reorganized company, but (unless for purposes for which first-mortgage bonds might otherwise have been issued) only after the concurring vote or consent of the holders of a

majority of the outstanding preferred stock. So far as permitted by law, such additional preferred stock may be of series A, or of any other series, one or more, and preferred stock of any such other series may bear dividends at such rate, cumulative or non-cumulative, may be redeemable or nonredeemable, convertible or non-[362] convertible, and may have such other rights and privileges and be subject to such limitations and restrictions, as may be from time to time determined by the board of directors prior to the issue of preferred stock of any such other series. If there are outstanding shares of preferred stock of different series, the earnings applicable to dividends thereon shall be apportioned among the respective series in proportion to the dividends accumulated on the shares of such series respectively.

In any liquidation or winding up of the reorganized company, whether voluntary or involuntary, the preferred stock shall be entitled to receive, out of the assets of the reorganized company, its par value, plus any accrued and unpaid cumulative dividends thereon, plus such premium, if any, as may be specified for any series, before any distribution shall be made on the common stock, but shall not be entitled to any further participation in such assets.

The reorganized company shall not, without the vote or consent of the holders of at least two-thirds in par value of the outstanding new preferred stock,

(1) create or permit to be created any mortgage or other lien upon any of its properties, excepting the new first mortgage, the new income mortgage, or purchase money liens (including equipment obligations) upon property hereafter acquired, given for not more than 75 percent of the purchase price of such property; (2) create or issue any bonds, notes, or other evidences of indebtedness maturing more than two years from their date, except new first-mortgage bonds and new income-mortgage bonds and except purchase money obligations given for not more than 75 percent of the purchase price of property hereafter acquired; (3) create any stock ranking, either as to assets or dividends, in priority to, or on a parity with, the new preferred stock, or (4) permit any subsidiary, all of the stock of which, except directors' shares, shall be owned by the reorganized company, to create any mortgage or other lien upon any of its properties or issue any such bonds, notes, or other evidences of indebtedness (except purchase money liens or obligations limited as aforesaid), or issue any additional stock of any class, unless the obligations secured by such mortgage or other lien or such other obligations or such stock shall be acquired by the reorganized company.

The preferred stock, series A, shall be entitled to receive all accumulated unpaid dividends and current dividends at the rate [363] of 5 percent per annum in respect of any calendar year before any dividends shall be paid or declared or set apart for payment on the common stock in respect of such



year. Such dividends shall be cumulative to the extent earned in any calendar year but not paid; but such dividends shall otherwise be noncumulative. For the purposes of the next preceding sentence hereinabove, preferred stock dividends shall be considered to be earned in any calendar year to the extent covered by the available net income for such year that remains after providing for prior charges (i.e., that remains after the deductions made pursuant to subparagraphs (1), (2), (3), (4), (5), and (6) of the fourth paragraph of subdivision L); or after the provisions of said subdivision L shall have ceased to be operative, to the extent covered by net income (as defined by the accounting rules or practice referred to in said subdivision L).

After dividends shall have been paid or declared, or set apart for payment, on the new common stock at the rate of \$3 a share in respect of any year, each share of preferred stock, series A, shall be entitled to share equally with each share of new common stock in any dividends paid or declared or set apart for payment, in respect of such year.

The preferred stock, series A, shall be redeemable, in whole or in part, at any time at its par value plus accrued and unpaid cumulative dividends, and proportionate dividend for the current year.

The holders of preferred stock, series A, shall not have any preemptive right to subscribe to any additional issues of stock of any class or of securities convertible into stock of any class.

Holders of preferred stock shall be entitled to one vote per share on all matters, except that in elections of directors, which shall be by cumulative voting, each holder of stock of either class shall be entitled to as many votes per share as the number of directors to be elected.

N. There will be authorized 1,000,000 shares of common stock, without par value, of which 319,441 shares are to be issued in the reorganization as set forth in subdivision P below and 424,382 shares shall be reserved for the conversion of income-mortgage bonds, series A. No new common stock additional to that actually issued in connection with the reorganization, as above [364] stated, shall be issued without the further authorization of this Commission or of such regulatory body or tribunal as may have jurisdiction thereof.

Holders of common stock shall be entitled to one vote per share on all matters except that directors shall be elected by cumulative voting as aforesaid.

So far as permitted by law, any vote or consent by the holders of common stock, authorizing the issue of additional shares of stock of any class or of securities convertible into stock of any class, may waive on such terms and conditions, if any, as may be specified in such vote or consent, the preemptive right of all the holders of shares of common stock to subscribe to such additional shares or securities.

O. The \$10,000,000 of new first-mortgage bonds, series A, to be authenticated and issued in the reorganization shall be sold at par and accrued interest

to the Reconstruction Finance Corporation (subject to the approval and authorization of this Commission and the delivery to the Reconstruction Finance Corporation of a legal opinion satisfactory to it as to the validity of the acquisition by the reorganized company of title to the properties of the debtor and the validity of the new first-mortgage bonds, series A, and the new first mortgage). In consideration of such purchase by the Reconstruction Finance Corporation of new first-mortgage bonds, series A, and considering the value of the collateral securing its claim, such claim amounting as of January 1, 1939, to \$3,862,870 (\$2,963,000 principal and \$899,870 interest) and represented by notes secured by general and refunding bonds of the debtor and other collateral, shall be provided for under the plan in like securities and in like proportions as those given holders of the debtor's first-mortgage bonds.

P. The existing securities of the debtor shall be treated as follows:

1. Existing equipment trusts, Baldwin lease, and Pullman contract, aggregating \$2,750,050 shall remain undisturbed and shall be assumed by the reorganized company.

2. Holders of existing first-mortgage bonds shall receive for each \$1,000, principal amount thereof, together with \$266.66 $\frac{2}{3}$  of [365] interest accrued and unpaid thereon to January 1, 1939, approximately \$400 of income-mortgage 4 $\frac{1}{2}$ -percent bonds, series A, (being 40 percent of the principal amount of said existing bonds); \$600 of 5-percent preferred

stock, series A (being 60 percent of the principal amount of said bonds); and 4.67 shares of common stock (being common stock taken at the price of \$57 a share for 100 percent of said accrued and unpaid interest).

3. The Reconstruction Finance Corporation shall receive in respect of the \$10,000,000 of new money provided for in subdivision O (or the surrender of trustees' certificates at their principal amount and accrued interest, to a like amount) and its existing claim in the principal amount of \$2,963,000, together with \$899,870 of interest accrued and unpaid thereon to January 1, 1939, approximately \$10,000,000 of new first-mortgage 4-percent bonds, series A (being 100 percent of said new money); \$1,185,200 of income-mortgage 4½-percent bonds, series A (being 40 percent of the principal of said claim); \$1,777,800 of 5-percent preferred stock, series A (being 60 percent of the principal of said claim); and 15,788 shares of common stock (being common stock taken at the price of \$57 a share for 100 percent of said accrued and unpaid interest).

4. The Railroad Credit Corporation shall receive in respect of its claim in the principal amount of \$2,455,610, together with \$146,503 of interest accrued and unpaid thereon to January 1, 1939 (subject to the reduction of said amounts by the application, prior to the date of issue of the new securities under the plan, of any proceeds from the distributive shares of the company or its subsidiaries

under the marshaling and distributing plan, 1931), approximately \$154,111 of income mortgage 4½-percent bonds, series A; \$241,681 of 5-percent preferred stock, series A; and 35,425 shares of common stock (being common stock taken at the price of \$62 per share). The Railroad Credit Corporation's equity in the collateral securing the claim of the Reconstruction Finance Corporation is found to be without value.

5. The A. C. James Company shall receive in respect of its claim in the principal amount of \$4,999,800, together with \$1,249,950 of interest accrued and unpaid thereon to January 1, 1939, [366] \$163,724 of income mortgage 4½-percent bonds, series A; \$256,756 of 5-percent preferred stock, series A; and 37,635 shares of common stock (being an amount of common stock which bears to the amount of common stock allotted to the claim of the Railroad Credit Corporation the same proportion that the principal amount of general and refunding mortgage bonds of the debtor held by the A. C. James Company as collateral for said claim, bears to the principal amount of such bonds held by the Railroad Credit Corporation as collateral for its claim).

6. The unsecured claims of the Western Pacific Railroad Corporation and the Western Realty Company, and other unsecured claims not entitled to priority over existing mortgages, are found to be without value, and no securities or cash shall be distributed under the plan in respect of these claims.



7. The capital stock of the debtor is found to be without equity or value, and the stockholders shall not be entitled to participate in the plan.

Q. Claims against the debtor entitled to priority over any mortgage of the debtor, current liabilities and obligations incurred by the trustees of the properties of the debtor during the reorganization proceeding, and expenses of reorganization allowed by the court within the maximum fixed by this Commission shall be paid in cash or assumed by the reorganized company, provided that any amounts so assumed by the reorganized company shall constitute a charge upon the properties of the reorganized company prior in lien to all new securities issued under the plan. When so treated, claims against the debtor entitled to priority over any of its mortgages are found not to be affected by the plan. Obligations under the debtor's equipment-trust certificates, the Baldwin lease, and the Pullman contract are found not to be materially and adversely affected by the plan. The reorganized company shall be deemed to have assumed the executory contracts of the debtor which by their terms do not terminate at or prior to the conclusion of the reorganization proceeding and which shall have been affirmed or shall not have been disaffirmed by the trustees of the properties of the debtor with the approval of the court prior to the confirmation of the plan, and also any executory contracts made by the trustees [367] of the properties with the approval of the court which by their terms do not ter-

minate at or prior to the conclusion of the reorganization proceeding.

R. The capital stock of the debtor and the unsecured claims against the debtor not entitled to priority over existing mortgages shall be canceled.

Existing mortgages on the debtor's properties shall be released and canceled, and all funds on deposit with the trustees under the debtor's mortgages representing sums paid from time to time to such trustees for the release of properties, sale of scrap, and otherwise, and all collateral pledged under the debtor's mortgages, shall be surrendered to the reorganized company free from liens of the debtor's mortgages, after deductions therefrom of any amounts which the court may find should be deducted under the provisions of such mortgages and consistent with this plan. All collateral pledged by the debtor as security for notes to the Reconstruction Finance Corporation, the Railroad Credit Corporation, and the A. C. James Company shall be reduced to possession by the respective pledgees thereof, and shall be by them surrendered to the reorganized company and canceled, except that the Railroad Credit Corporation shall not release or surrender any right or interest in the distributive shares of the debtor or its subsidiaries under the marshaling and distributing plan, 1931, but any proceeds from such distributive shares after the effective date of the plan shall become the property of and be retained by the Railroad Credit Corpo-

ration, but to the extent to which received prior to the issue of the new securities under the plan shall be applied in reduction of the claim of the Railroad Credit Corporation in respect of which such new securities are to be issued at the rates provided in subdivision P. The court by orders of March 11, 1936, and March 20, 1936, authorized the Chase National Bank of the City of New York to pay from funds which had been deposited with it by the debtor all outstanding first-mortgage bond coupons which matured on or prior to September 1, 1933, and had not theretofore been presented for payment. Any such coupons as shall not have been presented for payment up to the time of the consummation of the plan shall be paid in cash by the new company if and when presented by the holders thereof. [368]

The plan shall be carried out under the supervision of a reorganization committee consisting of three persons, all to be approved by the court, who shall be designated, one by the bondholders committee, one by the Reconstruction Finance Corporation, and one by the Railroad Credit Corporation and the A. C. James Company jointly. Should the bondholders committee, or the Reconstruction Finance Corporation, or the Railroad Credit Corporation and the A. C. James Company jointly, fail to designate a representative for membership on the committee within such time as the court shall consider reasonable, the court shall appoint such a representative.

The plan may be carried out either by revesting the properties formerly of the debtor in the debtor company or by transferring said properties to a new corporation organized for the purpose, and the execution by the corporation in which said properties are vested of the new mortgages and the issue by it of the new securities contemplated by the plan.

The method of carrying out the plan shall be determined by the reorganization committee in its discretion, and the reorganization committee shall also determine, subject to the approval of the court, the form, and, except as herein otherwise expressly provided, the provisions, of all mortgages, bonds, coupons, charters, by-laws, stock certificates, voting trust certificates, acceptances, assents, and all other instruments in the judgment of the reorganization committee necessary or desirable in connection with carrying out the plan.

The reorganization committee may act by a majority of its members as from time to time constituted, at a meeting or in writing without a meeting. The reorganization committee may employ such agents, attorneys, and others as it may deem desirable for the purposes of the plan. The reorganization committee may from time to time delegate to others any power or discretion conferred upon it by the plan; and the members of the reorganization committee shall not be liable for any action taken by them in good faith or by any person employed by the reorganization committee in good faith, ex-

cept for their respective individual malfeasance or wilful neglect.

Should the reorganization committee solicit deposits of securities, or authorization to represent holders of the debtor's existing [369] securities in the reorganization, the terms and conditions upon which such solicitation and representation would be made shall be subject to the prior approval of this Commission.

S. If deemed desirable and so ordered by the court, the plan, after it has been found fair and equitable and confirmed by the court, may be executed by a sale at not less than a fair upset price to be fixed by the court, of all or any part of the property of the debtor, all on such conditions and in such manner as the court may direct. Upon any such sale the property and assets offered for sale may be purchased for the benefit of the reorganized company by the reorganization committee, and in that event there shall be applied on account of the purchase price the distributive share of the proceeds of such sale of all securities the holders of which shall have assented to the plan, and of the securities, though not assenting to the plan, of all classes which shall have accepted the plan.

In the event of a sale of the properties of the debtor to the reorganization committee, the committee may in its discretion sell all or any portion of the new securities, if any, distributable under the plan to holders of existing securities, if neither



such security holder nor the class to which such security holder belongs shall have accepted the plan, provided that security holders in a class which shall not have accepted the plan, and who themselves shall not have accepted the plan shall have the right, if they shall so notify the committee within a period of 30 days after the confirmation of such sale, to assent to the plan and receive the securities allocated to them under the plan in lieu of their aliquot share of the proceeds of such sale of the properties. The proceeds of any such sale of securities may be used to pay the portion of the purchase price payable in cash on any such sale of the properties.

T. Unless otherwise provided in section 77 or any order or orders of the court in the reorganization proceeding or of this Commission, whenever notice shall be required or permitted to be given under or pursuant to the plan, such notice shall be given by publishing a copy of such notice once in each week on any secular day in each such week for two successive weeks in one newspaper published and of general circulation in the Borough of [370] Manhattan, City and State of New York, and in one newspaper published and of general circulation in the City of San Francisco, State of California, and also (1) in case of notices to security holders who have accepted the plan, by mailing such notice, postage prepaid, to the addresses of such security holders set forth in the acceptances signed by them; and (2) in case of notices to security holders who shall not have accepted the plan, by

mailing such notice, postage prepaid, to such security holders whose names and addresses appear on the books of the debtor or of the reorganized company, as the case may be, but failure to mail any such notices, or delay in mailing any such notices, shall not invalidate the notice by publication above provided for, which alone shall be sufficient.

U. The board of directors of the reorganized company shall consist of not less than 7 nor more than 11 members, who shall be elected by the holders of the preferred stock and the common stock of the reorganized company at an election to be held not later than 90 days after the consummation of the plan. Pending such election the board of directors shall consist of such persons as may be designated by the reorganization committee, with the approval of the court.

V. The construction of the plan by the court shall be final and conclusive. The court may cure any defect, supply any omission, or reconcile any inconsistency in such manner or to such extent as may be necessary or expedient in order to carry out the plan effectively.

W. Acceptance of the plan shall include acceptance of the new bonds, mortgages, stock certificates, and all instruments necessary and appropriate to the carrying out of the plan, other than the orders of the court and this Commission, to the same effect as though the terms of such instruments were set out in full herein.

Notwithstanding any other provisions of this modified order, the reorganized company shall as-

sume the liability for, and shall pay in full in due course, any and all taxes due to the United States from the debtor or the debtor's trustees for any taxable period prior to the date of the confirmation of the plan, whether [371] or not proof thereof has been made in the proceeding and without prejudice by reason of not having made proof thereof.

It is further ordered, That the authorization and approval herein granted by this Commission are upon the condition that the journal entries covering the necessary accounting adjustments under the order will be submitted to this Commission for approval before they are recorded on the books of the reorganized company under the plan of reorganization herein approved;

It is further ordered, That nothing herein contained shall be, or be construed as, a grant of authority for the issue of any securities, assumption of obligations, transfer of any property, sale consolidation, or merger of the debtor's properties, or pooling of traffic, pursuant to either the Bankruptcy Act or the Interstate Commerce Act, except as provided herein, or until further action by this Commission upon confirmation of the plan by the court; and

It is further ordered, That the order herein, dated October 10, 1938, be, and it is hereby, revoked.

By the Commission.

(Seal)

W. P. BARTEL,

Secretary.

[Endorsed]: Filed July 29, 1939. [372]

Before the  
Interstate Commerce Commission  
Finance Docket No. 10913

In the Matter of

THE WESTERN PACIFIC RAILROAD  
COMPANY,

Debtor.

EXCEPTIONS  
OF THE RAILROAD CREDIT CORPORATION,  
INTERVENOR, TO REPORT PRO-  
POSED BY THE BUREAU OF FINANCE  
AND  
SUPPORTING BRIEF

Comes now The Railroad Credit Corporation and excepts to the report proposed by the Bureau of Finance in the above entitled proceeding, and assigns the following errors:

1. That the Bureau erred in finding (p. 7) that the sum of \$58,566.12 was due from The Railroad Credit Corporation on November 30, 1936. (The date, 1916, in the report, was obviously intended to mean 1936.)

2. That the Bureau erred in failing to find that The Railroad Credit Corporation is entitled by the general law and by special contract to apply income and proceeds from collateral (including distributive shares under the Marshaling and Distributing Plan), to or towards the payment of princi-

pal or interest, or both, of and upon the obligations of the Debtor, in its untrammelled discretion.

3. That the Bureau erred in recommending (p. 50) that the Commission consider, for the purposes of a plan of reorganization, that the equipment covered by leases, conditional sale agreements or equipment trust agreements, is subject to the lien of the First Mortgage in priority to the General Mortgage. [400]

4. That the Bureau, although finding that the equity of the preferred and common stockholders of the Debtor has no value (p. 55), and that claims of several general creditors should be cancelled, nevertheless erred in recommending the issuance of warrants to The Western Railroad Corporation, one of the general creditors and stockholders of the Debtor, enabling it to purchase at par, within sixty days, all or any part of the \$10,000,000 of new first mortgage bonds, receiving a bonus of 10 shares of new common stock with every \$1,000 bond so purchased.

5. That the Bureau erred in recommending (p. 40) the immediate sale of \$10,000,000 of new First Mortgage Bonds, necessitating the payment of interest thereon, although it does not appear that said sum is presently required.

6. That the Bureau erred in failing (p. 54) to accord full recognition to all the collateral held by The Railroad Credit Corporation, in the allocation of new securities.

7. That the Bureau erred in failing to find that important and valuable items of collateral were



assigned to and pledged with The Railroad Credit Corporation by others than the Debtor, and cannot be taken from The Railroad Credit Corporation in this proceeding.

8. That the Bureau erred in proposing that the claim of The Railroad Credit Corporation against the Debtor be discharged.

9. That the Bureau's proposals are unfair, and unjustly discriminatory and prejudicial to the rights and interests of The Railroad Credit Corporation.

10. That the Bureau erred in proposing (p. 60) as the effective date of a plan of reorganization, January 1, 1937, a date already passed. [401]

#### BRIEF

1. That the Bureau erred in finding (p. 7) that the sum of \$58,566.12 was due from The Railroad Credit Corporation on November 30, 1936. (The date, 1916, in the report, was obviously intended to mean 1936.)

The figure given doubtless related to the undistributed book balance of the Debtor in the fund established under the Marshalling and Distributing Plan, 1931; but, as appears from said Plan, said undistributed book balance does not represent an amount due from The Railroad Credit Corporation to the Debtor; The Railroad Credit Corporation's only obligation in this respect being to credit to the account of the Debtor such sums, if any, as The Railroad Credit Corporation may find in its

hands in excess of its requirements in administering said Plan and said fund; moreover, the amount of said undistributed book balance is currently reduced as distributions are made, the undistributed book balance at date hereof being \$52,074.17.

2. That the Bureau erred in failing to find that The Railroad Credit Corporation is entitled by the general law and by special contract to apply income and proceeds from collateral (including distributive shares under the Marshalling and Distributing Plan), to or towards the payment of principal or interest, or both, of and upon the obligations of the Debtor in its untrammelled discretion.

See decision of District Court of United States, District of Connecticut, in *Re Reorganization of New York, New Haven & Hartford Railroad Company*; not yet reported, but printed at pp. 2689-2697, 2829-2830, and 2903-2904 of the record in said proceeding, filed with the Interstate Commerce Commission.

In consequence of applications made since the close of the hearing herein, the obligations of the Debtor have been further reduced, the amount [402] thereof on September 15, 1937, being

Principal .....	\$2,445,609.88
• Interest .....	67,836.33
Total .....	\$2,513,446.21

Note: In view of the reduction of the rediscount rate of the Federal Reserve Bank in the New York District, from  $1\frac{1}{2}\%$  to  $1\%$  in August, 1937, that

interest rate, unless sooner changed, will be applied by The Railroad Credit Corporation under the terms of the Marshalling and Distributing Plan, 1931, effective October 1, 1937.

3. That the Bureau erred in recommending (p. 50) that the Commission consider, for the purpose of a plan of reorganization, that the equipment covered by leases, conditional sale agreements or equipment trust agreements, is subject to the lien of The First Mortgage in priority to the General Mortgage.

In support of this exception, The Railroad Credit Corporation refers to the exceptions and supporting brief filed herein by the trustee of the General Mortgage. The Railroad Credit Corporation adopts all said exceptions, and the supporting brief, to the same extent as though set out herein at length.

4. That the Bureau, although finding that the equity of the preferred and common stockholders of the Debtor has no value (p. 55), and that claims of several general creditors should be cancelled, nevertheless erred in recommending the issuance of warrants to The Western Pacific Railroad Corporation, one of the general creditors and stockholders of the Debtor, enabling it to purchase at par, within sixty days, all or any part of the \$10,000,000 of new first mortgage bonds, receiving a bonus of 10 shares of new common stock with every \$1,000 bond so purchased.

If the value of the new common stock is sufficiently low to make the combined value of a new

\$1,000 first mortgage 4% bond and ten shares of  
[403]

stock approximate the purchase price of \$1,000, there must clearly be an over-issue of stock. It must be assumed, however, that the Bureau has found that there is sufficient property to support fully not only the other stock provided for, but also the \$10,000,000 of common stock proposed to be allotted as a bonus with the \$10,000,000 of new first mortgage bonds. If such value exists, as a basis for this stock, creditors senior to The Western Pacific Railroad Corporation are entitled to it. In any event, the holder of the warrants for new bonds will secure two dollars in securities for every dollar of investment: this is incongruous, even if lawful, in a re-organized corporation. It can scarcely be claimed that first mortgage 4% bonds, in the amount of only \$10,000,000 upon a property which the Bureau proposes to capitalize at more than \$90,000,000, and which even through the worst years of the depression, has earned sums available for interest more than sufficient to cover the interest requirements upon such bonds, must be "sweetened" by the addition of stock of an equal liquidating value, or, indeed, by the addition of any stock.

If the estate of the Debtor is insufficient to support this additional \$10,000,000 of stock, then, to the extent that such deficiency exists, the stock will be watered. In this connection, it is of interest to note that the Bureau found that if the \$10,000,000 of bonus stock is issued, the Debtor's estate is not sufficient to support the issue to The Railroad Credit

Corporation of stock having a par value equal to the amount of The Railroad Credit Corporation's claim, even though that claim is secured *inter alia* by general mortgage bonds in a principal amount nearly double the amount of the claim. If there is insufficient equity for mortgage bonds, there must of necessity be insufficient equity for general creditors: no general creditor is thus entitled to participate. [404]

It is significant that the Bureau proposes to allot to Reconstruction Finance Corporation common stock having a par value nearly double the amount of the claim: since we must assume that the Bureau would not propose giving to Reconstruction Finance Corporation securities worth more than the amount of the claim, it follows that, in the opinion of the Bureau, the new common stock, though it may be worth less, cannot be worth more than roundly \$50 a share. It also follows that The Railroad Credit Corporation is offered stock having, at most, a value of not more than half its claim: and yet the Bureau proposes to give something of value out of the Debtor's estate to The Western Pacific Railroad Corporation, whose position is junior to that of The Railroad Credit Corporation. Such a proposal might stand, on composition principles, if every creditor assented, but if a single creditor dissented, the proposal would necessarily be rejected by the court as being contrary to the requirements of Section 77. The allocation of the bonus stock to the secured note holders would patently be more equitable than the Bureau's proposal.



In either event, the Bureau's proposal would result in an unfair and unsound distribution of securities.

The Bureau's proposal tends not only to discredit other securities of the new company, but to discredit even the new first mortgage bonds themselves. It would be preferable to adjust the interest rate on the new bonds, to the market, or to sell those bonds at a discount. It is possible that satisfactory terms could be made for a loan in the full amount from Reconstruction Finance Corporation, without any increase in the rate of interest.

Even if the proposed issue of bonus stock is legal; it may well be that its issue as "fully paid" would subject the purchaser to an assessment in the event of subsequent financial difficulties. See *Brockett v. Winkle Terra Cotta Company*, 81 F. (2d) 949 (C. C. A. 8th, 1936); and *Spencer v. [405] Anderson*, 222 Pac. (Cal.) 355 (1924). The mere possibility of such an assessment would depress the market value not only of the bonus stock, but of all the remaining common stock.

It is obvious that if such an offer as is proposed to be made to The Western Pacific Railroad Corporation is to be made to any general creditor, it should be made on equal terms to all general creditors: certainly there is no basis for offering \$20,000,000 par value of securities to a single general creditor having a claim amounting to but a fraction of that sum. It would appear, that such an offer, if made at all, should be made first to prior creditors

whose claims are not satisfied by the proposals of the Bureau.

It should be noted, moreover, that The Railroad Credit Corporation is the holder of \$5,494,722 (plus interest), or substantially all, of the claim that is made on the basis of the proposed allocation of warrants to The Western Pacific Railroad Corporation, amounting to \$5,747,560, plus interest. If the possession of that claim justifies the proposed offer of warrants, that offer should be extended to The Railroad Credit Corporation rather than to The Western Pacific Railroad Corporation.

The further proposal of the Bureau, that said warrants be offered to Reconstruction Finance Corporation, The Railroad Credit Corporation and A. C. James Company, pro rata, in the event and to the extent that they are not taken up by The Western Pacific Railroad Corporation, is wholly illusory: it is obvious that if the warrants have value, the Western Pacific Railroad Corporation will exercise them to the extent, if any, that it is able and willing to do so, and sell the remainder to others. Obviously no part of the warrants will descend to The Railroad Credit Corporation if there is value in them; The Railroad Credit Corporation cannot expect to secure any right to such warrants unless they are entirely worthless. [406]

The proposed allotment of warrants opens the door to full ultimate recovery by The Western Pacific Railroad Corporation: that door is simultaneously closed to The Railroad Credit Corporation,

although the latter has a position senior to the former.

5. That the Bureau erred in recommending (p. 40) the immediate sale of \$10,000,000 of new First Mortgage Bonds, necessitating the payment of interest thereon, although it does not appear that said sum is presently required.

It may well be that before all of this sum is required, conditions may be such that first mortgage bonds of the character here proposed, will sell at their face value or even at a premium, without being bolstered by stock. In any event, it would seem unwise to saddle the new corporation with unnecessary interest charges.

6. That the Bureau erred in failing (p. 54) to accord full recognition to all the collateral held by The Railroad Credit Corporation, in the allocation of new securities.

The allocation proposed is based solely on holdings of general mortgage bonds. In addition, The Railroad Credit Corporation also holds (1) pledge of interest accrued upon said general mortgage bonds; (2) assignments of advances to the Debtor by three subsidiaries of the Debtor; (3) assignment of distributive shares of Debtor, and of two subsidiaries of the Debtor, under the Marshalling and Distributing Plan; (4) "negative pledge" of dividends on stock; and (5) equity in collateral pledged with Reconstruction Finance Corporation.

In this respect the Bureau's proposal, if carried

out, would be confiscatory. See comments under Paragraphs 9 and 10, *infra*. [407]

7. That the Bureau erred in failing to find that important and valuable items of collateral were assigned to and pledged with The Railroad Credit Corporation by others than the Debtor, and cannot be taken from The Railroad Credit Corporation in this proceeding.

The items referred to are as follows:

(a) \$2,000,000 principal of Debtor's general and refunding bonds;

(b) Assignment of distributive shares of two subsidiaries of the Debtor, under the Marshalling and Distributing Plan, 1931;

(c) Assignment of certain advances made by The Western Pacific Railroad Corporation to (I) the Debtor, (II) Sacramento Northern Railroad Company, and (III) Standard Realty and Development Company, respectively.

8. That the Bureau erred in proposing that the claim of The Railroad Credit Corporation against the Debtor be discharged.

The Railroad Credit Corporation holds as partial security for its claim against the Debtor, three items of collateral pledged with it by The Western Pacific Railroad Corporation, one item pledged with it by the A. C. James Company, and the distributive shares (under the Marshalling and Distributing Plan, 1931) of two subsidiaries of the Debtor. A pledge of collateral by a third person

is analogous to a guaranty, being in practical effect a guaranty limited to the value of the property pledged. The discharge of the claim of The Railroad Credit Corporation would terminate these several pledges. The right to retain a lien until the debt secured thereby is paid, is a substantive right which may not be taken from the creditor consistently with the Fifth and Fourteenth Amendments to the Constitution. *Security-First National Bank v. Rindge Land & Navigation Co.*, 85 F. (2d) 557 (C.C.A. 9, 1936). This rule is especially applicable when the pledge is given by third parties. In this respect the situation is closely parallel to that presented in *In Re Nine North Church Street* 85 F. (2d) 186 (C.C.A. 2nd, 1936). As there [408] intimated, the liquidation of said collateral may be essential to a reorganization of the Debtor. The Railroad Credit Corporation is ready and willing to liquidate said collateral on a proper basis. See also *In re Deversey Bldg. Corporation*, 85 F. (2d) 456 (C.C.A. 7th, 1936)..

Moreover, although The Railroad Credit Corporation has the legal right to sell any collateral pledged with it by third parties, there is doubt whether it could surrender, under any plan of reorganization, any collateral pledged with it by third parties, including, of course, the \$2,000,000 principal amount of general mortgage bonds of the Debtor pledged with The Railroad Credit Corporation by the A. C. James Company, unless such third party pledgors assented thereto. Furthermore, while The



Railroad Credit Corporation has the legal right to sell the \$2,000,000 principal amount of said bonds pledged with it by the Debtor, and upon which Reconstruction Finance Corporation has a second lien, it is doubtful whether The Railroad Credit Corporation would have the right to surrender said bonds under any plan of reorganization, unless the Reconstruction Finance Corporation had assented thereto. The Reconstruction Finance Corporation would be likewise restricted in its dealings with collateral upon which The Railroad Credit Corporation has a second lien.

9. That the Bureau's proposals are unfair, and unjustly discriminatory and prejudicial to the rights and interests of The Railroad Credit Corporation.

To the extent that the claim of The Railroad Credit Corporation is secured, it is entitled to treatment on a parity with other equally secured creditors, including in that category the holders of first mortgage bonds. See *In re New York, New Haven & Hartford Railroad Co.*, 16 F. Suppl. 504 (D.C., D. of Conn., 1936); also, comment under Paragraph No. 5, above. [409]

The Bureau's proposal:

(a) fails to recognize all of the collateral held by The Railroad Credit Corporation;

(b) allocates to The Railroad Credit Corporation securities having a value of less than half the amount of its claim;

(c) provides for the discharge of the claim of The Railroad Credit Corporation, so as to

deprive The Railroad Credit Corporation of collateral pledged with it by third persons;

(d) allocates valuable rights and interests in property of the Debtor to a general creditor, although the prior claim of The Railroad Credit Corporation has not been fully satisfied;

(e) allocates property to a general creditor based on a claim that had been assigned by that creditor to The Railroad Credit Corporation;

(f) provides for the issuance of stock upon terms that result in the dilution of what value there might otherwise be in the stock assigned to The Railroad Credit Corporation;

(g) recommends the issue of warrants for new first mortgage bonds and stock on a basis that dissipates assets of the Debtor, places an unnecessary interest charge on the Debtor, and discredits all securities issued by the Debtor under the proposed plan of reorganization; and

(h) deprives The Railroad Credit Corporation of income and proceeds of collateral to which it is lawfully entitled pending the consummation of a plan of reorganization. (See Paragraph No. 10, below).

Such treatment is confiscatory and contrary to the provisions of section 77 of the Bankruptcy Act, as well as in violation of the law of the land.

10. That the Bureau erred in proposing (p. 60) as the effective date of a plan of reorganization, January 1, 1937; a date already passed.

The Railroad Credit Corporation since that date has applied, and in duty bound will continue to apply, in accordance with its legal rights, income and proceeds from collateral, including distributive shares of the Debtor under the Marshalling and Distributing Plan. See also comment under Paragraph No. 2. [410]

Wherefore, The Railroad Credit Corporation, because of each and all of the errors herein specified, prays that the report proposed by the Bureau of Finance be so amended, as to correct the errors hereinabove specified, in the manner hereinabove set forth.

Dated: Washington, D. C., September 25, 1937.

Respectfully submitted,

D. WILLARD, JR.,

General Counsel,

The Railroad Credit Corporation.

Office and P. O. Address:

D. WILLARD, JR.,

805 Transportation Building,  
17th & H Streets, Northwest,  
Washington, D. C.

[Endorsed]: Filed Oct. 5, 1939. [411]

Before the  
Interstate Commerce Commission  
Finance Docket No. 10913.

THE WESTERN PACIFIC RAILROAD COM-  
PANY REORGANIZATION

EXCEPTIONS OF RECONSTRUCTION FI-  
NANCE CORPORATION TO THE PRO-  
POSED REPORT OF THE BUREAU OF  
FINANCE.

Reconstruction Finance Corporation (hereinafter called "Reconstruction"), an intervenor in the above-entitled proceeding, hereby makes and presents the following exceptions to the report proposed by the Bureau of Finance:

1. The report errs in failing to give any recognition to the accrued unpaid interest on the General and Refunding Mortgage Bonds (hereinafter called "Refunding Bonds") of the Western Pacific Railroad Company (hereinafter called "the Debtor") held by Reconstruction.
2. The report errs in failing to give any recognition to the substantial additional collateral security held by Reconstruction other than Refunding Bonds.
3. The report errs in failing to give any recognition to the claim which Reconstruction has for the deficiency, if any, on [412] its notes, after a sale or determination of the value of its collateral.
4. The report errs in giving to Western Pacific Railroad Corporation, an unsecured creditor, the

right to subscribe to \$10,000,000 principal amount of new First Mortgage Bonds and to receive in addition to said bonds a bonus of \$10,000,000 par value of new common stock.

5. The exceptions filed by Irving Trust Company, trustee of the Debtor's General and Refunding Mortgage, are concurred in by Reconstruction, which hereby adopts such exceptions as supplemental and additional exceptions.

6. If the Commission approves the plan proposed by the report, it will be unable to give the approval required by Section 5b(3) of the Reconstruction Finance Corporation Act, as amended.

7. The plan proposed by the report is unfair and inequitable to Reconstruction, fails to afford due recognition to its rights as the holder of an entire class of claims, discriminates unfairly against such class, and fails to conform to the requirements of the law of the land.

### I.

The report errs in failing to give any recognition to the accrued unpaid interest on the General and Refunding Mortgage Bonds of the Western Pacific Railroad Company held by Reconstruction.

Since the treatment of Reconstruction in the plan recommended by the Bureau of Finance is based entirely on the total amount of Debtor's Refunding Bonds held by Reconstruction, obviously such [413] treatment should recognize the rights given



by the covenants of the Bonds to the holders of such Bonds to be paid the principal thereof together with interest as specified in the Bonds. This the Bureau has failed to do and has given consideration merely to the principal amount of the Bonds without considering the unpaid interest. This constitutes error, since unpaid interest is as much of a debt as the principal.

That Reconstruction is a pledgee holding Refunding Bonds of the Debtor furnishes no reason why Reconstruction's right to treatment based on a calculation of the unpaid interest accrued on the Bonds should be ignored, since it is the universal rule that a pledgee—until satisfaction of the debt secured by pledged collateral—is entitled not only to the proceeds but the income of the pledged collateral.

In the present case the notes executed by the Debtor to Reconstruction were delivered in the State of New York and the loans evidenced by said notes were made in the State of New York. Furthermore, said notes are payable in the State of New York. In such circumstances, the law of New York is controlling with respect to the parties to the pledge contract, i. e., Reconstruction and the Debtor. See the following cases: *Burns Mortgage Co. v. Fried* (1934), 292 U. S. 487; *Dale v. Pattison* (1914), 234 U. S. 399, 404; *Taney v. Penn. Nat. Bank* (1914), 232 U. S. 174; *Hiscock v. Varick* [414] *Bank* (1907), 206 U. S. 28; *Cook v. Moffatt* (1847), 5

How. (46 U. S.) 295, 307; *Lee v. State Bank and Trust Co.* (1930), 38 F. (2d) 45, 47.

The right of a pledgee to income or proceeds of pledged collateral, until the satisfaction of the debt for which the collateral is pledged, is well recognized in the State of New York. See the following cases: *Brightson v. Claflin* (1919), 225 N. Y. 469, 122 N. E. 458; *D. S. Stern & Co. Inc. v. Pisitz* (1934), 270 N. Y. S. 715; *Manufacturers Trust Co. v. Bank of Yorktown* (1935), 282 N. Y. S. 507, 509; *In re Brewer's Estate* (1931), 253 N. Y. S. 213; *Ross v. Mabbett Motor Car Co. Inc.* (1922), 194 N. Y. S. 200.

While the Debtor was not in default on its notes held by Reconstruction, Reconstruction allowed it to pay to itself the interest as it matured on the \$10,750,000 principal amount of Refunding Bonds pledged with Reconstruction. Accordingly, the interest was so paid on said bonds to March 1, 1934. Since that date interest has been accruing at the rate of 5 per cent per annum, none of which has been paid or collected. As of January 1, 1938 (before which date the reorganization of the Debtor cannot be effected) there will be accrued and unpaid on the notes of the Debtor held by Reconstruction, \$2,150,000 of interest as follows, viz.:

Principal amount of Bonds	Series	Interest from March 1, 1934 to January 1, 1938
\$8,750,000	A	\$1,750,000
2,000,000	B	400,000
Total		\$2,150,000

This sum, \$2,150,000, when added to the principal amount of the bonds pledged with Reconstruction, \$10,750,000, amounts to \$12,900,000, which latter amount (with an additional adjustment for such further unpaid interest as shall have accrued on the pledged bonds at the date the plan is actually made effective) should serve as the basis for the issuance of securities to Reconstruction on account of the Refunding Bonds pledged with it.

Under the Bureau's proposal, the accrued unpaid interest on the First Mortgage Bonds is added to the principal amount of said Bonds as a basis for calculating the treatment to be given such bondholders. The Bureau's failure to add such interest in the case of the Refunding Bonds constitutes an inequitable discrimination against Reconstruction and the other pledgees of the Refunding Bonds in favor of the holders of the First Mortgage Bonds.

## II.

The report errs in failing to give any recognition to the substantial additional collateral security held by Reconstruction other than Refunding Bonds.

As already referred to, the treatment proposed in the report for Reconstruction's claim is based entirely upon the principal amount of \$10,750,000 of Refunding Bonds pledged with Reconstruction. In addition to such principal amount of bonds Reconstruction holds substantial additional collateral security consisting [416] of (1) 150,000 shares, or

one-half, of the outstanding common stock of Denver and Rio Grande Western Railroad Company, represented by voting trust certificates, and (2) a second lien upon \$2,000,000 principal amount of Refunding Bonds held in pledge by The Railroad Credit Corporation. Obviously, the report errs in failing to give any recognition to this additional collateral security.

Since the report contemplates the extinction of Reconstruction's claim on its notes and the surrender of the collateral therefor, the acceptance by Reconstruction of the plan proposed in the report would automatically release from pledge the additional items of collateral security (1) and (2) above. The proposed plan is confiscatory to the extent that it fails to give any recognition to such additional collateral security.

The Denver and Rio Grande Western stock, regardless of its intrinsic value, is of considerable value strategically, since through the stock control is exercised over the Denver and Rio Grande Western Railroad Company, an essential link in the transcontinental route consisting of the Western Pacific, the Denver and Rio Grande Western, and the Missouri Pacific systems. The disposition of this stock vitally affects both the Missouri Pacific and Western Pacific interests. See petition and brief dated September 3, 1937, filed by the Missouri Pacific Railroad Company for reconsideration of its petition for leave to intervene. This [417] stock

was pledged with Reconstruction by the Western Pacific Railroad Corporation. Unless the latter corporation releases Reconstruction, this stock will have to be returned by Reconstruction to the Western Pacific Railroad Corporation. For such return Reconstruction, under the proposed plan, will receive no equivalent consideration. A fair and equitable plan either would assign to Reconstruction, in consideration of the return of this stock to Western Pacific Railroad Corporation, an equivalent part of the securities which would otherwise be accorded to the Western Pacific Railroad Corporation: or, would provide that Reconstruction may sell this stock, in its untrammelled discretion, for such price as it can obtain for the stock. Failure to do so constitutes a discrimination against Reconstruction, in favor of the Western Pacific Railroad Corporation.

A somewhat different situation exists as to the \$2,000,000 principal amount of Refunding Bonds on which Reconstruction has a second lien. Should Reconstruction not accept the plan proposed in the report and The Railroad Credit Corporation, on the other hand, do so. The Railroad Credit Corporation, the holder of the senior lien, will be under a legal duty to turn over to Reconstruction the \$2,000,000 principal amount of [418] bonds. The Railroad Credit Corporation is likewise under a legal duty to surrender the bonds to Reconstruction (and not to the Debtor) upon satisfaction of its claim by payment out of the proceeds of its other col-



lateral, or otherwise than by the acceptance of new securities under the proposed plan. Reconstruction's right to the bonds, in any of these eventualities, is a valuable property right; and the failure of the report to give any recognition to such right, in the circumstances herein involved, is unjustly discriminatory and prejudicial to the interests of Reconstruction.

### III.

The report errs in failing to give any recognition to the claim which Reconstruction has for the deficiency, if any, on its notes, after a sale or determination of the value of its collateral.

It is elementary that to the extent, if any, Reconstruction is not fully secured, Reconstruction is a general creditor for the deficiency. It is likewise elementary that all general creditors must be treated alike.

That these elementary principles are applicable to a Section 77 proceeding, plainly appears from *In re New York, New Haven & Hartford Railroad Co.*, 16 F. Supp. 504 (D.C., D. of Conn., Sept. 16, 1936) where Judge Hincks stated (p. 509):

"\* \* \* as observed earlier in this memorandum, under the Act only a plan which is free from confiscatory features may be confirmed. To be sure, under the Act the court may approve a plan modifying or altering [419] the rights of creditors generally, or of any class of them, secured or unsecured, etc. But since only an

equitable plan may be approved, the plan must provide that every creditor in the order of his priority shall receive under the plan rights which in equity are the fair equivalent of such of his rights as have been subjected to equitable modification, at least in so far as the assets of the debtor's estate permit. *Any creditor found to be only partially secured is entitled to the equitable equivalent of such security as he has, with a right to share in equality with common creditors for the excess of his claim as allowed above the value of his security as ascertained by equitable considerations.* And the plan must recognize the prior right of common creditors with respect to such assets as remain after equitable treatment has been accorded to secured creditors. *Kansas City Ry. v. Central Union Trust Co., 271 U. S. 445.* Such is the intent of the Act: \* \* \* (Italics ours.)

The Bureau's report violates these principles. It fails to find that Reconstruction's claim is fully secured. On the contrary, it does not make any finding whatever as to the extent to which Reconstruction's claim is secured; and in view of the allocation against the claim of new common stock only, we must conclude that the Bureau is of the view that Reconstruction and the other collateral noteholders (who are less well secured than Reconstruction) are all inadequately secured and that such collateral noteholders, including Reconstruc-

tion, have deficiencies on their respective notes. To the extent of such deficiencies, they are, accordingly, general creditors of the Debtor, and must be accorded equal treatment with the Debtor's other general creditors. Yet the report gives a single general creditor, the Western Pacific Rail- [420] road Corporation, the warrant rights hereinafter more fully discussed, without recognizing in any way the claims of the collateral noteholders as general creditors to the extent, if any, of their respective deficiencies.

This treatment is unfair and inequitable. Likewise it fails to afford due recognition to the rights of Reconstruction and discriminates unfairly against it. If the secured creditors are only partially secured and have deficiency claims for the balance—this the Bureau assumes to be clearly so in the case of The Railroad Credit Corporation and the A. C. James Co., since they are given common stock of a less par value than the face amount of their claims—then, if, as the Bureau's plan also assumes, there is not a sufficiency of value to recognize the deficiency claims, there can be no justification for giving anything, under the plan, to The Western Pacific Railroad Corporation. Neither can there be any such justification, if such assumptions are correct, unless and until Reconstruction's claim is satisfied in full. [421]

## IV.

The report errs in giving to the Western Pacific Railroad Corporation, an unsecured creditor, the right to subscribe to \$10,000,000 principal amount of new First Mortgage Bonds and to receive in addition to said bonds a bonus of \$10,000,000 par value of new common stock.

Although the Bureau states that "The Commission should find that the equity of the preferred and common stockholders of the Debtor has no value" (p. 55) and although it recommends that the unsecured, general claim of the Western Realty Company should be cancelled (p. 55), it then proceeds to give to the Western Pacific Railroad Corporation (which holds stock and also an unsecured note of the Debtor), warrants to purchase at any time within sixty days after the reorganization is effected, \$10,000,000 of new First Mortgage 4% Bonds which (except for equipment trusts) will be the only fixed interest obligation of the reorganized company and will have an absolute first lien on the Debtor's entire system, valued by this Commission at approximately \$145,000,000. In addition, the purchaser of the new First Mortgage Bonds of the reorganized company will be entitled to receive as a bonus \$10,000,000 aggregate par value of common stock.

This treatment is subject to the following objections for reasons predominately of a business nature:

a. The record does not show any need for the immediate sale, upon reorganization, of \$10,000,000 of new First Mortgage [422] Bonds, necessitating the payment of interest thereon from the date of their issuance. The Bureau's recommendation is not supported by any finding of such necessity.

b. The report proposes that the new bonds will be part of a proposed authorized issue of \$50,000,000 of such bonds. As mentioned heretofore, such bonds would constitute the only fixed interest obligation of the reorganized company, except for equipment trusts. Whether or not the Bureau had a purpose in making the amount of the authorized issue of new bonds substantially the same as the amount of the outstanding First Mortgage Bonds now in default, does not appear. At any rate, the record fails to disclose any necessity or justification for such a large authorized issue of new bonds. The authorized amount should be cut down to but a fraction of the figure proposed. In addition, the new mortgage should provide restrictions, not proposed in the report, against the issuance of additional bonds when there is insufficient earnings coverage. Otherwise, the Bureau's proposal is but an invitation to the reorganized company to repeat the process, in which the Debtor has indulged, of overloading the property with debt and fixed interest charges—the cause of the present bankruptcy.



c. The Bureau's proposal to issue a bonus of \$10,000,000 [423] of stock with the new bonds tends not only to discredit the new bonds themselves, but also all of the other securities issuable under the plan. If the new bonds cannot be sold at their principal amount with a 4% coupon rate, and without any stock bonus, it would be preferable to adjust the interest rate on the new bonds.

Apart from the above, the Bureau's proposal to allot \$10,000,000 of new common stock as a bonus with \$10,000,000 of new First Mortgage Bonds is subject to other fatal objections. As shown by the record (see Exhibit 2), Reconstruction on July 20, 1935 was willing, provided the approval of the Interstate Commerce Commission was obtained, to accept new securities for its present debt and to put \$10,000,000 of new money into the property, as needed, taking therefor either at their face amount \$10,000,000 of new First Mortgage Bonds carrying an interest rate of 4 per cent for the first ten years and  $4\frac{1}{2}$  per cent thereafter; or a twenty-year or twenty-five-year 4% note secured by bonds of the same issue on a basis of 120 per cent of the amount borrowed. As shown by the Debtor's plan, these bonds were to be part of no less than some \$25,000,000 of new First Mortgage Bonds to be issued upon reorganization. With an issue of only \$10,000,000 of new First Mortgage Bonds constituting a first lien on properties valued at about

\$145,000,000 it is highly probable that the holder of the warrants for the new bonds will be able to [424] make arrangements through private banking channels for a syndicate to take the bonds off his hands at their face amount and resell them to the public at the face amount or better, thus leaving the warrant holder with the bonus of \$10,000,000 of new common stock for which he has paid nothing whatsoever. Bearing upon this probability, it should be kept in mind that the Debtor's rehabilitation program instituted during the reorganization period has called for abnormally large expenditures which have reduced substantially the Debtor's net income available for fixed charges. Upon the completion of such program the effect of these expenditures should be just the opposite. The economies which the Debtor should be able to realize from the improvements made should be reflected in substantially better earnings. Likewise, increased traffic may reasonably be expected from the Northern California Extension and the Dotsero Cut-off, both of which were completed during the depression.

It must be assumed that the Bureau *if* of the opinion that there is value to support both the issue of \$10,000,000 of new First Mortgage Bonds and \$10,000,000 of new common stock. If there is such value, then, as pointed out above, the holder of the warrants will receive under the proposed plan \$2.00 worth of new securities for each \$1.00 of new money put in the property. Unless and until senior creditors are satisfied, there can be

no justification for singling out one of the general creditors, the Western Pacific Railroad [425] Corporation, and affording it more advantageous treatment than is afforded secured creditors.

On the other hand, if there is not value in the Debtor's estate sufficient to support the \$10,000,000 of new common stock, then to the extent of the deficiency in value, there will be a watering of stock, with consequent dilution of the value of the stock to be issued to the First Mortgage bondholders and the collateral noteholders. There is no provision of Section 77 which allows the Commission to authorize an issue of watered stock. In this respect, Section 77 is like Section 77B. Watered stock, issued in a reorganization under either section, will, even if legally issued, be subject to the claims of creditors of the reorganized company. This point was decided by the Circuit Court of Appeals for the Eighth Circuit in *Brockett v. Winkle Terra Cotta Company* (1936), 81 Fed. (2d) 949, a case involving a Section 77B reorganization. In its decision that court held (p. 959):

"We have been referred to no case where stock has been permitted to be issued 'without the shadow of right or consideration' and where it 'does not represent actual or substituted value in corporate assets.' It is, of course, urged that the cancellation of the bonded indebtedness constitutes a consideration for the stock issued to the bondholders. This may be true as between the corporation and assenting stock-

holders, but it cannot be held binding upon creditors who deal with the company upon the faith of its capital stock. No new money or its equivalent accrues to the Terra Cotta Company by virtue of the transaction. Not a dollar has been added to the physical assets of the Corporation by this additional stock issue. [426]

One who assents to that issue and accepts the certificates stands in the same relationship to the public as that assumed by an original subscribing stockholder. \* \* \*

"And it is the avowed purpose of the plan to seek credit and to borrow money upon the faith of this stock issue. It is not proposed to offer that stock for sale upon the market at its real worth. As stated in the plan, 'it is believed' \* \* \* that its financial position would justify a line of bank credit sufficient to prepare for, make up, and fill any orders it may be able to obtain.' The witness Davis, on behalf of the debtor-petitioner, says: 'It seems to me this company can handle its credit situation by getting rid of this bond issue and then going to the banks on its individual orders.' By this means, notwithstanding the fact that the terra cotta business is admitted to be at a standstill, two other local companies being out of business or in liquidation, it is hoped 'that the company will be able to endure the loss of business incident to the economic depression for a few more years.'

"We may lay on one side the question of whether the financial responsibility of stock in an uncertain business venture may fairly be substituted for a first mortgage lien against the protest of the lienor. The paramount question here is whether these objecting bondholders may be forced into the position of holders of stock issued for an inadequate consideration, and thereby exposed to possible if not probable financial responsibility and loss. We do not think so. Without impugning the motives of the proponents of the plan, we feel that potentially it may affect injuriously the rights of creditors and of the public generally, and is, therefore, nonfeasible and unfair to these objectors as well. The small value of the physical property involved, and the large percentage of acceptance on the part of the stockholders and bondholders, no doubt operated in the trial court to obscure this issue which, we think, conditions the disposition of this appeal."

For a California decision (under the laws of which the Debtor Railroad is incorporated, see *Spencer v. Anderson* (1924) [427] 222 Pac. 355, where the Court recognized the liability of the holder of watered stock to creditors, saying in part (p. 357):

"\* \* \* the creditor does not stand in the shoes of the corporation and he is not suing to recover upon a claim of the corporation against the stockholder. He may recover, though the



corporation have no such claim. His action is not upon a debt due from the stockholder to the corporation. It is to recover compensation for a wrong done directly to him by the corporation acting for the stockholder and participated in by the latter. The gist of the creditor's action is that he was induced to extend credit to the corporation by the false representations of the corporation respecting the amount paid in by the stockholder to the corporate capital, and the measure of his recovery is the same as in ordinary actions for damages for deceit, namely, the difference between the amount which has actually been paid in by the stockholder to the corporate capital and the amount which would have been paid in had the representations been true."

If the Commission is of the view that warrants should be issued in the reorganization to any of the parties, they should be offered first to secured creditors whose claims are not satisfied by the Bureau's proposal. The proposed plan would give one of the unsecured creditors, ~~The Western Pacific Railroad Corporation~~, as a bonus or gift, \$10,000,000 par value of new common stock, against \$7,188,607 of debt, including interest (Report, p. 24), while the General Mortgage bondholders, who are secured, would receive new common stock for their bonds, on the basis of dollar for dollar. This is essentially unfair. The Bureau's proposal that if The Western Pacific Railroad Corporation does not

within sixty days [428] exercise the warrants, they will then be offered to Reconstruction, The Railroad Credit Corporation, and the A. C. James Company, pro rata, is unrealistic. If the warrants are of any value (and there is justification for belief that they will have substantial value), then they will either be exercised by The Western Pacific Railroad Corporation or sold by it to investment bankers or other purchasers. Obviously, no part of the warrants will accrue to Reconstruction if they have any value. Reconstruction cannot reasonably expect to receive any of the warrants unless at the time the reorganization is effected they are completely valueless.

#### V.

The exceptions filed by Irving Trust Company, Trustee of the Debtor's General and Refunding Mortgage, are concurred in by Reconstruction, which hereby adopts such exceptions as supplemental and additional exceptions.

Reconstruction adopts all of the exceptions filed by Irving Trust Company, Trustee of the Debtor's General and Refunding Mortgage, and said Trust Company's supporting brief, to the same extent as though set out herein at length.

On the basis of the said exceptions, it is obvious that Reconstruction is entitled to securities of the reorganized company on a substantially more favorable basis than are the holders of the Debtor's First Mortgage Bonds. This is for the reason that, as said Trust Company sets forth, the Refunding

Bonds are secured by a first [429] lien on substantial properties of the Debtor of a value in excess of the amount of Refunding Bonds outstanding; and Reconstruction's claim, in turn, is secured by Refunding Bonds of a principal amount in excess of three times the amount of Reconstruction's claim. Clearly, if the exceptions of said Trust Company are well taken, as we believe them to be, Reconstruction's claim is more than 100% secured.

## VI.

If the Commission approves the plan proposed by the report, it will be unable to give the approval required by Section 5b(3) of the Reconstruction Finance Corporation Act, as amended.

It should not be forgotten that both the Commission and the Directors of Reconstruction, found, in 1932 and 1933, at the time that the Reconstruction loans were made, and when the earnings of the Debtor Railroad were much less favorable than they are to-day, that with the collateral security required by the Commission, Reconstruction would be adequately secured. Western Pacific Railroad Company Reconstruction Loans, 180 I.C.C. 645, 184 I.C.C. 699, and 189 I.C.C. 575.

Likewise, it should not be forgotten that, in addition to any duties imposed upon it by Section 77 of the Bankruptcy Act, a special duty with respect to the claim of Reconstruction in the [430] reorganization is imposed upon the Commission by Section

5b(3)\* of the Reconstruction Finance Corporation Act, as amended. Under the latter section, Reconstruction has no power to accept for its present claim new securities, except "with the prior approval of the interstate Commerce Commission." This provision is an integral part of the Reconstruction Finance Corporation Act, as amended, and is a limitation upon the powers of Reconstruction. Obviously, its purpose was to insure, by requiring the prior approval of the Commission, that Reconstruction's claim should receive adequate treatment

---

\* This section provides as follows:

"(3) In connection with the reorganization under section 77 of the Federal Bankruptcy Act, approved July 1, 1898, as amended, or with receivership proceedings in a court or courts, of any railroad or railway indebted to the Corporation or any railroad or railway the receivers or trustees of which are indebted to the Corporation, the Corporation may, *with the prior approval of the Interstate Commerce Commission*, adjust or compromise its claim against such railroad or railway, or any such receiver or trustee, by accepting, in connection with any such reorganization or receivership proceedings and in exchange for securities or any part thereof then held, new securities which may have such terms as to interest, maturity, and otherwise as may be approved by the Corporation, or part cash and part new securities so approved: Provided, That any such adjustment or compromise shall not be made on less favorable terms than those provided in the reorganization of the railroad or railway for holders of claims of the same class and rank as the claim of the Corporation." (Italics ours). [431]

in a Section 77 proceeding or in an equity receivership. Under the provision, the responsibility is imposed upon both the Commission and Reconstruction to make certain that Reconstruction does receive such adequate treatment.

It is respectfully submitted that if the Commission approves the Bureau's plan, it will not be able to give the approval required by Section 5b(3) of the Reconstruction Finance Corporation Act, as amended.

## VII.

The plan proposed by the report is unfair and inequitable to Reconstruction, fails to afford due recognition to its rights as the holder of an entire class of claims, discriminates unfairly against such class, and fails to conform to the requirements of the law of the land.

Neither the Commission nor the Court can approve a plan which does not conform to the requirements of Section 77. Subsection (d) of Section 77 provides that the Commission, if it approves any plan whatsoever, shall approve a plan "that will in its opinion meet with the requirements of subsections (b) and (e)" of Section 77, "and will be compatible with the public interest." Subsection (e) of Section 77 provides in part that "the judge shall approve the plan if satisfied that: (1) it \* \* \* is fair and equitable, affords due recognition to the rights of each class of creditors and stockholders, does not discriminate unfairly in favor of any class of creditors or stockholders, and will conform to the requirements of the law of the land regarding



the participation of the various classes of creditors and stockholders \* \* \*."

These requirements, as we have already shown, are not met [432] by the plan proposed in the Bureau's report. Incidentally, the District Court, in classifying creditors and stockholders, has put Reconstruction in a class by itself, so that the failure of the Bureau's plan to give due recognition to the rights of Reconstruction constitutes a failure to afford due recognition to an entire class of creditors. Likewise, the unfair discrimination of the proposed plan against Reconstruction is an unfair discrimination against an entire class of creditors. Yet, even if the claims of Reconstruction, The Railroad Credit Corporation, and the A. C. James Company, in respect of the Refunding Bonds, were consolidated into a single class, Reconstruction's claim would amount to 56.6 per cent. of the class.

It is respectfully submitted that the proposed plan, even if approved by the Commission, could not be approved by the Court. For the reason that it could not be approved by the Court, it should not be approved by the Commission.

Oral argument is requested.

Respectfully submitted,

C. M. CLAY,

Assistant General Counsel

W. MEADE FLETCHER, JR.,

Counsel

Attorneys for Reconstruction Finance Corporation  
Of counsel:

CLAUDE E. HAMILTON, JR.,

General Counsel

[Endorsed]: Filed Oct. 5, 1939. [433]

Before the  
Interstate Commerce Commission

Finance Docket No. 10913

In the Matter  
of

The Western Pacific Railroad Company  
Reorganization

EXCEPTIONS OF THE DEBTOR TO THE  
PROPOSED REPORT OF THE BUREAU  
OF FINANCE AND BRIEF IN SUPPORT  
OF ITS EXCEPTIONS. [434]

## TABLE OF CONTENTS

	Page of Original Printed Document	Page of Printed Record
Exceptions .....	1	447
Brief .....	4	449
I. The Report Errs in Failing to Approve a Practicable Plan of Reorganization Reason- ably Acceptable to Security Holders as a Composition Under Section 77 of the Bank- ruptcy Act .....	4	449
II. The Report Errs in Attempting to Limit Total Capitalization to \$91,406,510. by Authorizing in Addition to Existing Obli- gations to be Assumed in Reorganization not more than \$10,000,000. of First Mort- gage Bonds, \$19,716,040. of 50 Year In- come Mortgage 4% Bonds; 295,740-3/5 Shares of Preferred Stock, and 800,682-1/5 Shares of Common Stock .....	5	450
III. The Report Errs in Construing Section 77 of the Bankruptcy Act as a Mandate or Legislative Declaration that Capitalization shall "not Exceed a Conservative Valua- tion of the Assets to be Taken Over by the Reorganized Company" .....	12	458
IV. The Report Errs in Disregarding the Sec- tion 19a Value of the System Properties Amounting as of December 31, 1935, to \$144,619,851. ....	13	459
V. The Report Errs in Refusing to Authorize the Issue of Stock Without Par Value and in Treating No. Par Value Stock at \$100. Per Share in Measuring Capitalization .....	14	460

VI. The Report Errs in Providing for the Expropriation of the Collateral or the Debtor's Interest in the Property Represented by the Collateral Securing the Debtor's Notes Held by Reconstruction Finance Corporation, The A. C. James Co. and The Railroad Credit Corporation.....	19	466
VII. The Report Errs in Assuming that the Public Interest Involves Matters Lying Beyond the Field of Transportation and Includes the Amount of Interest Charges Which are not Fixed Obligations to Pay but are Payable Only Out of Available Income; Sound Financing; Financing Through Junior Obligations and Other Phases of Controversial Economics.....	21	467
VIII. The Report Errs in Proposing a Finding That the Equity of the Preferred and Common Stockholders of the Debtor has no Value .....	22	469
IX. The Report Errs in Failing to Find That the Debtor's Plan is Fair and Equitable and Otherwise Complies with the Provision of Section 77 and is Compatible With the Public Interest .....	24	471

Appendix

The High Function of the Interstate Commerce Commission is to Approve a Plan of Reorganization Compatible with the Public Interest Designed to Command the Support of the Percentages of Each Class of Creditors and Stockholders Necessary to Make a Binding Composition Under Section 77 of the Bankruptcy Act Which Contemplates the Relief and not the Elimination of the Debtor .....	31	478
--	----	-----

## TABLE OF CASES

	Page of Original Printed Document	Page of Printed Record
Acquisition and Operation of Fellsmere Railroad by Trans-Florida Central Railroad Company, 124 I. C. C. 366 (1927).....	17	463
Acquisition of Control of Seaboard Air Line Rail- way, 131 I. C. C. 733 (1927).....	17	463
Algers, Winslow & Western Railway Company Securities, 166 I. C. C. 788 (1930).....	15	461
Atlanta, Birmingham and Coast Railroad Com- pany v. United States, 296 U. S. 33 (1935).....	13	459
Chicago, Milwaukee & St. Paul Reorganization, 131 I. C. C. 673 (1928).....	16	462
Cincinnati, Georgetown Railroad Company Ac- quisition and Operation, 166 I. C. C. 134 (1930).....	15	461
Continental Illinois Bank and Trust Company v. Chicago, Rock Island and Pacific Railway Com- pany, 294 U. S. 649.....	4, 31	478
Cook Transit Corporation Stock, 202 I. C. C. 465 (1934).....	15	461
Cumberland Glass Co. v. DeWitt, 237 U. S. 447; 265 U. S. 269.....	36	484
Dayton-Goose Creek Railway Company v. U. S., 263 U. S. 456.....	22	468
Delaware & Northern Railway Company Stock, 162 I. C. C. 187 (1930).....	16	462
Denver & Salt Lake Railway Company Control, 170 I. C. C. 4 (1930).....	18	464



	Page of Original Printed Document	Page of Printed Record
Denver and Salt Lake Reorganization, 117 I. C. C. 397 (1926) ; 117 I. C. C. 749 (1927).....	17, 19	463, 464 [437]
iv		
East Washington Railway Company Acquisition and Stock; 212 I. C. C. 516 (1936). Commis- sioner Porter dissenting.....	15	461
Finance Application of Delaware & Hudson Com- pany and Delaware & Hudson Railroad Corpo- ration, 158 I. C. C. 615 (1930).....	16	462
Grand Trunk Western Railroad Company Stock, 162 I. C. C. 540 (1930).....	16	462
Great Northern Railway Company Securities, 212 I. C. C. 327 (1936).....	15	461
In re H. J. Arrington Co., 113 Fed. 498.....	36	484
Kansas City, Mexico & Orient Reorganization, 145 I. C. C. 339 (1928).....	16	462
Kansas City Terminal Railway Company, et al. v. Central Union Trust Company of New York, et al., 271 U. S. 445.....	33	480
Louisiana & Arkansas Railway Company Stock, 217 I. C. C. 208 (1936).....	15	461
Minneapolis, Anoka & Cuyuna Range Railroad Company Stock, 170 I. C. C. 591 (1931).....	15	461
Missouri-Kansas Belt Railway & Terminal Com- pany, Proposed Construction, Etc., 207 I. C. C. 175 (1935).....	15	461
Nassau Smelting & Refining Works, Ltd. v. Brightwood Bronze Foundry Company, 265 U. S. 269.....	36	484

	Page of Original Printed Document	Page of Printed Record
New York Central Railroad Company Securities, 221 I. C. C. 269 (1937).....	14	460
New York Central Railroad Company Securities, 199 I. C. C. 546 (1934). (Stock changed from \$100. par to no par value).....	15	461
Ohio & Morenci Railroad Company Stock, 199 I. C. C. 7 (1933).....	15	461
		[438]
v		
In re Realty Associates Securities Corp., 6 Fed. Supp. 549; 295 U. S. 295.....	36	484
Reorganization and Control of Atlanta, Birming- ham & Atlantic Ry. Co., 117 I. C. C. 439 (1926)	17	463
St. Louis & Troy Railroad Company, et al. Ac- quisition and Construction, 189 I. C. C. 464 (1933).....	15	461
San Diego & Arizona Eastern Railway Company Acquisition and Stock, 187 I. C. C. 713 (1932)	15	461
Savannah & Atlanta Railway Company Acqui- sition and Securities, 166 I. C. C. 119 (1930).....	16	462
Savannah & Atlanta Railway Company Acqui- sition and Securities, 162 I. C. C. 771 (1930).....	16	462
Seaboard Air Line Railway Company Readjust- ment, 158 I. C. C. 182 (1929) modified in 162 I. C. C. 267 (1930).....	16	462
Securities and Acquisition of Control of Railway Express Agency, Incorporated, 150 I. C. C. 423 (1929).....	16	462
Securities of Mayo & Cook's Hammock Railroad Company, 154 I. C. C. 622 (1929).....	16	462

	Page of Original Printed Document	Page of Printed Record
--	--	------------------------------

Sexton v. Lloyd's Bank, Ltd., 219 U. S. 339.....	23, 27	469, 474
--	--------	-------------

Stock of Castelman River Railroad Company, 158		
--	--	--

I. C. C. 149 (1929).....	16	462
--------------------------	----	-----

Stock of Port Angeles Western Railroad, 145		
---	--	--

I. C. C. 144 (1928).....	16	462
--------------------------	----	-----

Stock of Santa Fe, San Juan & Northern Rail- road, 154 I. C. C. 741 (1929).....	16	462
--	----	-----

In re Waynesboro Drug Co., 157 Fed. 401.....	36	484
--	----	-----

[439]



## EXCEPTIONS.

The Western Pacific Railroad Company, the Debtor herein, hereby excepts to the proposed Report of the Bureau of Finance filed herein on or about August 2, 1937, and respectfully submits the following exceptions to said proposed Report (herein called "~~the~~ Report"): [440]

### I.

The Report errs in failing to approve a practicable Plan of Reorganization reasonably acceptable to security holders as a composition under Section 77 of the Bankruptcy Act (pp. 59, 60).

### II.

The Report errs in proposing to limit total capitalization to \$91,406,510. (p. 46) by authorizing in addition to existing obligations to be assumed in reorganization not more than \$10,000,000. of First Mortgage Bonds (p. 39), \$19,716,040. of 50 Year Income Mortgage 4% Bonds (p. 43), 295,740-3/5 shares of Preferred Stock (p. 44), and 300,682-1/5 shares of Common Stock (p. 44).

### III.

The Report errs in construing Section 77 of the Bankruptcy Act as a mandate or legislative declaration that capitalization shall "not exceed a conservative valuation of the assets to be taken over by the reorganized Company" (p. 36).

### IV.

The Report errs in disregarding the Section 19a



value of the System properties amounting as of December 31, 1935, to \$144,619,851. (p. 23).

#### V.

The Report errs in refusing to authorize the issue of stock without par value and in treating no par value<sup>o</sup>[441] stock at \$100. per share in measuring capitalization (p. 36).

#### VI.

The Report errs in providing for the expropriation of the collateral, or the Debtor's interest in the property represented by the collateral, securing the Debtor's notes held by Reconstruction Finance Corporation, the A. C. James Co. and The Railroad Credit Corporation (p. 54).

#### VII.

The Report errs in assuming that the public interest involves matters lying beyond the field of transportation and includes the amount of interest charges which are not fixed obligations to pay but are payable only out of available income (p. 37); sound financing (p. 38); financing through junior obligations and other phases of controversial economics (p. 42).

#### VIII.

The Report errs in proposing a finding that the equity of the preferred and common stockholders of the Debtor has no value (p. 55).

#### IX.

The Report errs in failing to find that the Debtor's Plan is fair and equitable and otherwise com-

plies with the provisions of Section 77 and is compatible with the public interest (pp. 36, 37).

[442]

## BRIEF.

### I.

The Report Errs in Failing to Approve a Practicable Plan of Reorganization Reasonably Acceptable to Security Holders as a Composition Under Section 77 of the Bankruptcy Act.

From the tenor of the Report it is clear that the Bureau of Finance misconceives the true function of the Interstate Commerce Commission under Section 77, which is to reconcile differences between security holders so as to make practicable a composition under Section 77 and not to rewrite the Debtor's capital structure.

In *Continental Illinois Bank and Trust Company v. Chicago, Rock Island & Pacific Railway Company* (294 U. S. 648), the United States Supreme Court, referring to the original Section 77, said:

"As outlined by that section, a plan of reorganization, when confirmed, cannot be distinguished in principle from the composition with creditors authorized by the act of 1867, as amended by the act of 1874." (p. 672)

To this end subsection (d) of Section 77 requires that a Plan of Reorganization shall be set down for hearing unless the Interstate Commerce Commission shall consider it to be "*prima facie impracticable.*"

Obviously the Commission, if it is to make Section 77 a workable statute, if it is to develop a Plan that will bring the property of the Debtor out of the courts and restore it to private operation, ought not itself [443] to report a Plan which, if it were proposed by the Debtor or by a group of creditors, it would be the duty of the Commission to dismiss because impracticable.<sup>1</sup>

## II.

The Report Errs in Attempting to Limit Total Capitalization to \$91,406,510. By Authorizing in Addition to existing Obligations to Be Assumed in Reorganization Not More Than \$10,000,000. of First Mortgage Bonds, \$19,716,040. of 50 Year Income Mortgage 4% Bonds, 295,740-3/5 Shares of Preferred Stock, and 300,682-1/5 Shares of Common Stock.

Nowhere in the Act do we find any authority or jurisdiction conferred upon the Interstate Commerce Commission to limit *capitalization*\* and to prescribe the amount and character of the securities which a corporation reorganized thereunder shall be permitted to issue.

The lesser authority—the authority to limit fixed charges—is given *expressly* by subsection (b) but

---

<sup>1</sup> A further interpretive discussion of Section 77 appears in the Appendix.

\* Italics used in this brief are by counsel for Western Pacific Railroad Company.

must be exercised subject to and in conformity with a prescribed statutory formula. It would, therefore, be contrary to familiar rules of statutory construction to assume that a greater authority—the authority to limit the amount and character of *all* forms of capital securities—is given (a) not expressly but only by implication and (b) to be exercised not according to [444] formula or statutory guide but in the uncharted discretion of the Interstate Commerce Commission.

**\$10,000,000. principal amount of First  
Mortgage Bonds.**

We agree that it is within the province of the Interstate Commerce Commission to say that the reorganized Company shall not issue more than \$10,000,000. of First Mortgage 4% Bonds, either (a) because fixed charges under the formula prescribed in subsection (b) ought not to exceed \$400,000. (a conclusion we think would be erroneous) or (b) because a first lien on the rails ought to be reserved exclusively as a credit basis for new money (a position asserted by the A. C. James Co. but which we think is not sustained by the record in this case).

The public interest requires that carriers engaged in interstate commerce be assured of new capital on reasonable terms and in certain cases it may be necessary to reserve an exclusive first lien on the rails to attract new capital.

Such cases are, however, the exception and not

the rule and the present case, we submit, is governed by the rule and not by the exception.

In presenting the Debtor's "earnings experience" the System Income Account for the fourteen years period 1922 to 1935 was introduced, showing average annual income available for interest of \$2,165,920.<sup>2</sup> Deferred maintenance of \$5,036,778. existing on January 1, 1936, was assumed to have accrued during this period reducing the average to \$1,800,000. or more than 1.7 times the fixed charges proposed by the Debtor and [445] more than  $4\frac{1}{2}$  times the fixed charges proposed by the Bureau of Finance.<sup>3</sup>

The true earnings are depressed in the Bureau's Report by substituting for the fourteen years period 1922-1935 as the Debtor's "earnings experience" the ten years period 1926-1935, thereby giving greater effect to the low depression period earnings and reducing the average to \$1,207,100., assuming (which is *not* the fact) that all deferred maintenance accrued during this ten year period.

The Report then refers to tax burdens under the Social Security Act and the Railroad Retirement Act, which if applied retroactively would have amounted to \$537,653. in 1930, \$488,633. in 1931, \$365,498. in 1932, \$331,149. in 1933, and \$257,345. in 1934, asserts that similar data is lacking for the full ten years period, but states

---

<sup>2</sup> Tr. p. 221.

<sup>3</sup> Tr. pp. 215, 216; Ex. 23.



"it is apparent that such amounts should be considered in determining the debtor's probable future earnings available for interest and dividends."<sup>4</sup>

At a later point, however, the Report states,

"\* \* \* But, limitation of the fixed charges of the reorganized company on the basis of such hypothetical adjustments can hardly be justified, since other factors, now unknown, tending to increase net earnings may later affect the situation."<sup>5</sup>

In attempting to limit fixed interest charges to less than, \$500,000 the Report seems to rest entirely [446] upon the depression years of 1931, 1932 and 1933, and in so doing

(a) it *ignores* the fact that the 1931 deficit is a nonrecurring incident of the rapidly changing operating conditions peculiar to that period and that total Operating Revenues in that year which yielded no profit amounted to \$14,852,938, whereas in 1934, with Operating Revenues of only \$13,779,237, there was income available for interest of \$1,084,243.85;

(b) it *erroneously assumes* that the 1932 income of \$252,706. was a deficit, thus understating the reported income by \$515,412, and,

(c) it *entirely disregards* the controlling fact that the reported incomes for these years do not

---

<sup>4</sup> Report, pp. 19-21.

<sup>5</sup> Report, p. 39.

contain the revenue of the Northern California Extension as a seasoned line and an established route.<sup>6</sup>

We respectfully urge that the Bureau of Finance was not justified in ignoring the estimate of Charles Elsey, President of the Debtor, who testified that in any future depression equally as severe as that of 1931, 1932 and 1933, the earnings from this new line will not fall below \$2,961,853. and that in any such future depression the System earnings available for interest would not fall below \$1,218,000.<sup>7</sup>

As already pointed out we are working under a composition statute which aims to bring about capital readjustments by agreement of creditors and stockholders in specified percentages. Success or failure easily may depend upon the allotment of a reasonable [447] proportion of fixed interest bearing bonds to our present First Mortgage Bondholders. 30% was the percentage originally agreed upon and we submit that this amount could properly be authorized (a) because an interest charge of \$1,027,036. is abundantly justified by the 1931-1934 income *plus* a very conservative estimate of earnings from the Northern California Extension, (b) because reserved Bonds under the First Mortgage after an initial issue requiring not more than \$1,027,036. to be paid as the annual fixed charge

---

<sup>6</sup> Report, pp. 38-40; Tr. p. 255.

<sup>7</sup> Tr. pp. 162, 163.

would be sound Bonds according to accepted standards and reasonably certain to attract sufficient new capital, and (c) because the primary purpose of Section 77 is to promote and not to prevent the prompt reorganization of rail carriers that are victims of the late depression.

**\$19,716,040. of 50 Year Income Mortgage  
4% Bonds.**

We cannot agree that it is within the province of the Interstate Commerce Commission to say that the reorganized Company shall not issue more than \$19,716,040. of Income Bonds. Such Bonds are not fixed interest bearing obligations and the public interest is not affected by the amount of Income Bonds which find their way into the capital structure of the reorganized Company but the public interest may be adversely affected if the present holders of our First Mortgage Bonds (many of whom are testamentary trustees or other fiduciaries, institutional investors, banks and insurance companies) are relegated to a stock position which in many jurisdictions they are not permitted to occupy and are required to [448] accept a form of security which they cannot hold and are obliged to sell. *A sound reorganization should include among its features every inducement to the old security holders to continue their investment in the new Company and not in effect merely pave the way for future involuntary liquidation.*

By consulting its own archives the Commission will find that it heretofore certified that it was

compatible with the public interest for the Debtor to issue actually or nominally \$49,290,100. of First Mortgage Bonds and \$18,999,500 of General and Refunding Mortgage Bonds, a total of \$68,289,600. of fixed interest bearing obligations, although it is now asked by the Bureau of Finance to say that only \$19,716,040. of this grand total is entitled to preserve its superior character as debt and that \$48,573,560.\* must be converted into stock.

How the Bureau of Finance reached the conclusion that only \$19,716,040. of Income Bonds should be issued is not clear but apparently has some relation to a capitalization of the 1936 reported income after deducting fixed interest and the \$500,000. capital fund.

As already noted there is nothing in Section 77 authorizing the Interstate Commerce Commission to limit or prescribe the character of the securities of the reorganized company except as expressly authorized in respect of fixed interest bearing obligations but even if such authority may be implied, it is manifestly unfair to holders of our First Mortgage Bonds to use 1936 income as a yardstick in view of the fact that the cycle of earnings is upward in transportation and nearly every other industry and in view of the further admitted fact that the construction of the Northern California Extension, a new and as yet undeveloped [449] property, has revolutionized the Debtor's earning power.\*

---

\*Tr. pp. 161-163; 255.

We do not overlook the argument that fifty years hence the reorganized company may be embarrassed by the maturity of this issue of Income Bonds. This, however, is not a substantial or practical reason which should be given weight as against the insistence of substantial holders of our First Mortgage Bonds that debt should be preserved as debt and not converted into a lower form of investment.

*Income Bonds should be authorized up to the full principal amount of First Mortgage Bonds, \$49,290,100. (or such part thereof as is not refunded in new First Mortgage Bonds) and despite the misgivings of the Bureau of Finance, we think that full interest upon these Income Bonds will be earned in 1938.\**

295,740-3/5 shares of Preferred Stock and

300,682-1/5 shares of Common Stock.

The major vice of the Report is the proposal to wipe out all of the equity and part of the lien investment in the property of the Debtor by refusing to authorize an issue of securities thereagainst. Instead of giving to the Debtor the relief contemplated by Section 77, i.e., a stake in the future

---

\* Note Exhibit 29. Statement No. 2, and monthly income statements subsequent to the last hearing filed under stipulation. Our estimate for 1938 is \$2,929,586. The estimate for 1936 was exceeded by \$242,546. Figures to date show an even greater improvement over the 1937 estimate. There is no reason whatever to doubt the integrity of the estimate for 1938.



prosperity of the property, the Bureau proposes a death sentence.

In justifying this result the Report states that the [450] debtor's forecasts of earnings are open to doubt but as one critic has well observed, "It might better have said, not subject to determination."

*Property rights ought not to be taken away or titles extinguished by mere appraisals of even present values; much less by estimates of future earnings. Such a result runs counter to all of our conceptions of due process of law.*

### III.

The Report Errs in Construing Section 77 of the Bankruptcy Act as a Mandate or Legislative Declaration that Capitalization Shall "Not Exceed a Conservative Valuation of the Assets to Be Taken Over by the Reorganized Company."

Nowhere in the Act is there any suggestion that the Interstate Commerce Commission should undertake to reduce, limit or otherwise deal with capitalization. To read into the Act as the Bureau of Finance attempts to do in this case a requirement that capitalization "shall not exceed a conservative valuation of the assets to be taken over by the reorganized Company" is to read into the Statute a provision which it does not contain and which is alien to its express and fundamental objectives.

The real intent is to keep alive and conserve potential values by averting a foreclosure or a permanent readjustment of capital on the basis of present day values. The Commission is expressly authorized by [451] the Act to judge the future by the past in limiting fixed charges, but there is no such authorization in respect of junior securities which involve no fixed interest obligations.

*Again we observe that appraisals of property values and earning power by a Bureau of the Government, however informed and impartial may be the judgment upon which such appraisals are based, cannot be accepted as a safe substitute for the traditional requirements of due process of law.*

#### IV.

The Report Errs in Disregarding the Section 19a Value of the System Properties Amounting as of December 31, 1935, to \$144,619,851.

For reasons above stated the Debtor contends that Section 77 does not authorize the Commission to fix, limit or otherwise deal with *capitalization*.

If, however, the Commission enters this field then we submit that it ought not except for the most cogent reasons and upon a clear and convincing record entirely disregard its own Section 19a valuation.<sup>1</sup>

Here the discrepancy between the capitalization proposed in the Report and the value placed by the Commission under Section 19a as the property in-

---

<sup>1</sup>Atlanta, Birmingham and Coast Railroad Company v. United States, 296 U. S. 33 (1935).

vestment upon which the carrier is guaranteed a fair return by the Fifth Amendment is so extreme, amount- [452] ing as it does to more than \$53,000,000, as to constitute a menace to the general rate structure.

Under-capitalization may be even more serious in its repercussions than over-capitalization, and we are confident that this strategic railway bridging the territory between the Great Salt Lake and the Pacific Ocean, and occupying what is perhaps the last available route through the Sierra Nevada Mountains but also serving a new and undeveloped territory lying to the north, should not be so re-capitalized as (a) to liquidate on the basis of present day depressed levels its undeterminable potential values, and (b) to set up in competition with its more prosperous neighbors a reorganized Company, which, because of excessive under-capitalization forced upon it by a governmental authority may do business profitably at less than the cost of the service.

#### V.

The Report Errs in Refusing to Authorize the Issue of Stock Without Par Value and in Treating No Par Value Stock at \$100. Per Share in Measuring Capitalization.

In the following cases the Interstate Commerce Commission has authorized the issue of stock without par value:

New York Central Railroad Company Securities, 221 I. C. C. 269 (1937).  
curities, 221 I. C. C. 269 (1937) [453]

- Louisiana & Arkansas Railway Company Stock, 217 I. C. C. 208 (1936).
- East Washington Railway Company Acquisition and Stock, 212 I. C. C. 516 (1936).  
Commissioner Porter dissenting.
- Great Northern Railway Company Securities, 212 I. C. C. 327 (1936).
- Missouri-Kansas Belt Railway & Terminal Company Proposed Construction, Etc., 207 I. C. C. 175 (1935).
- Cook Transit Corporation Stock, 202 I. C. C. 465 (1934).
- New York Central Railway Company Securities, 199 I. C. C. 546 (1934). (Stock changed from \$100. par to no par value).
- Ohio & Morenci Railroad Company Stock, 199 I. C. C. 7 (1933).
- St. Louis & Troy Railroad Company et al. Acquisition and Construction, 189 I. C. C. 464 (1933).
- San Diego & Arizona Eastern Railway Company Acquisition and Stock, 187 I. C. C. 713 (1932).
- Minneapolis, Anoka & Cuyuna Range Railroad Company Stock, 170 I. C. C. 591 (1931).
- Algers, Winslow & Western Railway Company Securities, 166 I. C. C. 788 (1930).
- Cincinnati, Georgetown Railroad Company Acquisition and Operation, 166 I. C. C. 134 (1930). [454]

Savannah & Atlanta Railway Company Acquisition and Securities, 166 I. C. C. 119 (1930).

Delaware & Northern Railway Company Stock, 162 I. C. C. 187 (1930).

Grand Trunk Western Railroad Company Stock, 162 I. C. C. 540 (1930).

Savannah & Atlanta Railway Company Acquisition and Securities, 162 I. C. C. 771 (1930).

Seaboard Air Line Railway Company Readjustment, 158 I. C. C. 182 (1929) modified in 162 I. C. C. 267 (1930).

Stock of Castleman River Railroad Company, 158 I. C. C. 149 (1929).

Finance Application of Delaware & Hudson Company and Delaware & Hudson Railroad Corporation, 158 I. C. C. 615 (1930).

Securities of Mayo & Cook's Hammock Railroad Company, 154 I. C. C. 622 (1929).

Stock of Santa Fe, San Juan & Northern Railroad, 154 I. C. C. 741 (1929).

Securities and Acquisition of Control of Railway Express Agency, Incorporated, 150 I. C. C. 423 (1929).

Kansas City, Mexico & Orient Reorganization, 145 I. C. C. 339 (1928).

Stock of Port Angeles Western Railroad, 145 I. C. C. 144, (1928).

Chicago, Milwaukee & St. Paul Reorganization, 131 I. C. C. 673 (1928). [455]



Acquisition of Control of Seaboard Air Line Railway, 131 I. C. C. 733 (1927).

Acquisition and Operation of Fellsmere Railroad by Trans-Florida Central Railroad Company, 124 I. C. C. 366 (1927).

Reorganization and Control of Atlanta, Birmingham & Atlantic Ry. Co., 117 I. C. C. 439 (1926).

Denver & Salt Lake Reorganization, 117 I. C. C. 397 (1926); 117 I. C. C. 749 (1927).

It is respectfully submitted that the Bureau of Finance is in error in this case (a) in not resorting to stock without par value as a sound and convenient method of keeping alive for the benefit of the junior creditors and stockholders the equity in this virile and resilient property and (b) in assuming that no par value stock if resorted to must be given a substantial value for the purpose of measuring capitalization.

From the foregoing incomplete but impressive list of precedents we select the first and the last as illustrating the usefulness of stock without par value.

The case first cited is that of the New York Central Railroad Company which, with the approval of the Interstate Commerce Commission, changed its \$100. par value Common Stock to no par value stock as an integral and indispensable part of a financial operation that saved one of the premier railroads of the United States.

The case last cited is that of Denver and Salt Lake Railroad Company, which was reorganized in 1926 on the basis of an issue of 50,000 shares of Common Stock [456] without par value. With the approval of the Interstate Commerce Commission the Common Stock was set up upon the books at \$5,000,000, "arrived at by adjusting book values to the basis of our tentative valuation, plus additions and betterments since the date of valuation". While the Commission expressly disclaimed any responsibility for the then book value of the stock, it is interesting to note that it subsequently authorized the purchase of the no par value stock by the Denver and Rio Grande Western Railroad Company at the price of \$150. per share.<sup>2</sup>

It is true that the unfortunate stockholders of the old Railroad Company were foreclosed and were not permitted to participate in the valuable equity that was conserved through the issue of the no par value stock of the new Railway Company but it was just such a case that Congress had in mind when it adopted Section 77 for the express purpose of relieving Debtors from the inequity of final capital adjustments on the basis of subnormal conditions.

There is no sanctity or virtue in stock having a par value or a book value of \$100. As already noted the capital stock of the New York Central Railroad Company is without par value. The stock of the

---

<sup>2</sup> Denver & Salt Lake Railway Company Control, 170 I. C. C. 4 (1930).

Pennsylvania Railroad Company has always been a \$50. par value stock and this is true of most rail carriers organized in Pennsylvania. In other fields stocks vary from no par or nominal (\$1.00) par value to \$10., \$20., \$25., \$50., \$100. and intermediate figures determined by the exigencies of each case.

[457]

Values change from day to day, from week to week and from year to year, and it is impossible to maintain any rational relationship between the property account and the capital stock and why therefore should the Commission try to fix a relation which almost immediately will begin to yield to the force of changing conditions.

The true course and the one plainly indicated by Section 77 is to preserve the positions of all creditors and stockholders and unless the case of the stockholder is hopeless (when he may be taken care of by purchase warrants) stock without par value should be allotted to the equity to give the equity holders a participation in any extraordinary prosperity that may develop in the future. The book value may be placed at \$1.00, or as was done in the case of the Denver and Salt Lake Railway Company, may be measured somewhat in relation to the 19a value of the System properties plus additions and betterments to the date of reorganization.<sup>3</sup>

---

<sup>3</sup> 117 I. C. C. at page 406.

## VI.

The Report Errs in Providing for the Expropriation of the Collateral or the Debtor's Interest in the Property Represented by the Collateral Securing the Debtor's Notes Held by Reconstruction Finance Corporation, the A. C. James Co. and the Railroad Credit Corporation.

Equity abhors a forfeiture.

So it is that properties are not foreclosed and property rights not forfeited without, [458]

(a) a reasonable nisi period within which the debtor may pay, and

(b) an opportunity to bid at a public sale, and

(c) a reasonable period thereafter within which to redeem.

The Report cuts off all of these rights by giving outright the collateral to the pledgees after first converting it into capital stock of the reorganized Company.

Such a procedure was not contemplated by Section 77 which, whatever may be its defects, was mindful of the solicitude of equity for redemption rights and in connection with a sale of property stipulates that it shall be "at not less than a fair upset price".

Here, however, all equity of the junior interests in \$18,999,500. of General and Refunding Bonds and other collateral securing the Notes held by Reconstruction Finance Corporation, A. C. James Co. and The Railroad Credit Corporation, is proposed to be wiped out without sale or upset price or right

of redemption. This we submit is contrary to the requirement of Section 77, the usages of equity and the established principles of due process of law.

Whatever Plan is ultimately adopted for the Debtor we submit that the secured Notes should be converted into some form of collateral note issue that will give effect to their present collateral position but will nevertheless afford the Debtor an opportunity to work out the problem over a period of years. The idea of giving Reconstruction Finance Corporation more, and the A. C. James Company less, than the face of their re- [459] spective claims cannot be justified by Section 77 or by the law of the land regarding the participation of creditors—especially since both the A. C. James Co. and The Railroad Credit Corporation have special or cross equities in the collateral held by Reconstruction Finance Corporation.

## VII.

The Report Errs in Assuming That the Public Interest Involves Matters Lying Beyond the Field of Transportation and Includes the Amount of Interest Charges Which Are Not Fixed Obligations to Pay But Are Payable Only Out of Available Income; Sound Financing; Financing Through Junior Obligations and Other Phases of Controversial Economics.

Subsection (d) of Section 77 expressly provides that the Interstate Commerce Commission may

“render a report and order in which it shall approve a Plan which may be different from any Plan which has been proposed.”



Literally construed this provision may be deemed to authorize the Commission to write its own Plan for any carrier and give effect to any views it may have on any features even though inherently controversial in their nature.

But when we consider that the objects of the Statute are the relief of debtors and, as pointed out by Mr. Justice Sutherland in his opinion in the Rock Island [460] case, a prompt reorganization of the property and its release from the Courts, the inevitable conclusion is that the Interstate Commerce Commission was expected to adhere somewhat closely to the trail blazed by the Act; that it was to concern itself primarily with the points that touch the public interest.

Of course, a determination of the permissible fixed charge is of prime importance and is to be dealt with by the Commission on the basis of a statutory formula. The only other requirement is that the Plan shall be in the public interest, which gives no new or extraordinary jurisdiction to the Commission but merely reasserts a jurisdiction that it has exercised in the authorization of securities ever since the enactment of the Transportation Act, 1920.<sup>4</sup> Here the public interest has always been understood to lie in the encouragement of an inflow of private capital that will insure an adequate transportation service.<sup>5</sup>

---

<sup>4</sup>Transportation Act, 1920, Sec. 20a.

<sup>5</sup>Dayton-Goose Creek Railway Company v. U. S., 263 U. S. 456.

## VIII.

The Report Errs in Proposing a Finding That the Equity of the Preferred and Common Stockholders of the Debtor Has No Value.

The Report finds the single sum value of the System properties as of December 31, 1935, to be \$144,619,851, on which date the indebtedness of the Company, exclusive of claims for interest, amounted to only \$69,071,271. Accrued interest was then less than \$6,461,469., so that [461] the total debt ahead of the stock was only \$75,450,640.<sup>6</sup> There was, therefore, an equity of more than \$69,169,211. represented by the Debtor's stock on the basis of the Commission's own valuation under Section 19a.

Although, as we have already pointed out, the Section 19a valuation may not be a criterion of value except as it fixes the amount upon which the carrier is given a constitutional right to a fair return, it is, nevertheless, made *prima facie* evidence and ought not to be cast aside to permit equities to be taken away on mere estimates and speculative forecasts.

Estimates were submitted by the Debtor which show a 4% on \$100,000,000. in 1940.<sup>7</sup> This was part of an estimate for a five year period of which one and one-half years have already elapsed during which elapsed period the actual results have greatly exceeded the estimates. Moreover, these estimates were prepared solely for the purpose of showing that \$1,027,031. would be a conservative fixed charge and not for the purpose of placing a limit of \$4,000,-

000, on the earning power of the property in 1940 or in any other period. When the estimates were made the Northern California Extension had barely emerged from the construction stage and there was no basis for a true appraisal of its earning power. Subsequent earnings show that the value of the north and south line, which opens up a new channel of trade between the Pacific Northwest and the System lying to the South and the East of the lines of the Debtor, was [462] greatly understated.<sup>6</sup> Should there be any disposition on the part of the Commission to make a finding that extinguishes nearly \$70,000,000. of property represented by the Commission's own 19a value; then we ask that this case be set for further hearing to enable the Debtor to meet an issue that it had never conceived it could be called upon to meet in this case—the issue of confiscation.

---

<sup>6</sup> The rights of the parties are fixed as of the date of bankruptcy. *Sexton v. Lloyd's Bank Ltd.*, 219 U. S. 339.

<sup>7</sup> Ex. 29, Statement No. 2. See also note 9 on page 11, (*supra*).

<sup>8</sup> Tr. p. 255.

